SVIA STABLE TIMES

Volume 4 • Issue 1 First Quarter 2000

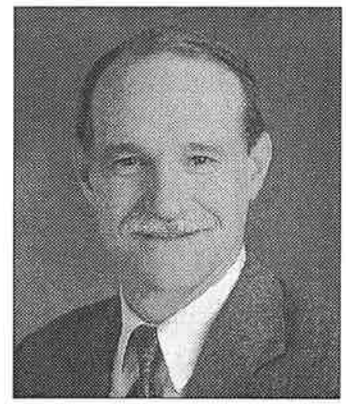
IN THIS ISSUE

ALSO IN THIS ISSUE

It's Easy to Sell High and Buy Low: Rebalance

By David L. Wray, Profit Sharing/401(k) Council of America

Early 401(k) critics stated that employees, especially lower-paid employees, would over trade their accounts and attempt to time the market. They predicted disastrous consequences both for individual employees and the retirement system. To paraphrase one of my good friends from Alabama "that dog just didn't hunt." In fact, most defined contribution plan participants have done just the opposite.



When employees join a plan they choose approximately three fund options (Table 1), that they never change, in which to invest their contributions. Even older employees, those with the largest account balances, typically do not make changes in how their balances are allocated. As you can see in Table 2, in 1998 most participants made no adjustments to their accounts.

Sell High, Buy Low *continued on page 3*

Performance Measurement Task Force Update

By Victoria Paradis, J.P. Morgan

Despite a proliferation in the number of task force members, we have come to solid consensus on many key performance measurement issues. Following is an update on the issues resolved and those still in progress.

CONCLUSIONS TO DATE

Performance measurement does not threaten the stable value industry. The idea of this project is to allow plan sponsors to "look under the hood" at the underlying portfolio results for all stable value fund assets. It does not jeopardize the book value returns that participants continue to earn. For example, performance measurement

Performance Measurement Task Force Update *continued on page 7*

Editor's Perspective

By Karl Tourville, Galliard Capital

Spring is definitely in the air. The weather is warming (even up here in Minnesota). The annual IIR GIC conference is right around the corner. Consumers are in a buying frenzy. Internet stocks continue their meteoric ascent. Y2K was a non-event. We've put together another content rich edition of Stable Times. If only Greenspan would quit trying to take the punch bowl away from the party!

Our first issue of the new millennium has a broad collection of timely, insightful pieces. Kicking it off, we have two articles relating to performance measurement. Vicky Paradis provides an update on the work of the Association's Performance Measurement Task Force, while Janet Jasin Quarberg discusses a new performance evaluation tool available to stable value investors developed by Hueler Analytics.

We also have several articles providing insight and interpretation of data relevant to stable value market participants. David Wray's article illustrates compelling data supporting the contention that participants need to be encouraged to rebalance their portfolios (lest the markets rebalance for them) while Dallas Salisbury takes a look at current asset allocations based on a database that accounts for 11% of all 401(k) plans and a quarter of all 401(k) participants and assets. Judy Markland's article provides insight on the interest rate policies pursued by different types of stable value managers. On the legal front, Al Turco discusses the implications of a recent Department of Labor (DOL) regulation designed to provide a "safe harbor" for the issuers of certain investment contracts while Don Myers highlights Congressional hearings on bringing ERISA into the new century.

All in all, a complete and comprehensive issue. Enjoy the issue, enjoy the spring, and we hope to see you in Palm Springs. (Let's also hope for a return to positive cash flows!)

New Hire at SVIA

SVIA welcomed Jennifer Hudson aboard this month as the new Communications Officer.

Jennifer is a graduate of Pacific University located in Forest Grove, Oregon. For the past year, she has served as Assistant Press Secretary for Senator Gordon H. Smith, (R-OR). Her previous experience includes public relations work with Pac/West Communications where she coordinated several political campaigns including two candidate races and two state-wide ballot measures. In addition to the hands-on public relations experience, she brings strong html and web-design skills.

Jennifer was chosen out of 47 applicants. Six individuals were interviewed. The field was narrowed down to two finalists, who were then interviewed by Kim McCarrel and Bill Gardner.

Stable Times Newsletter, SVIA's web-site and promotional materials for the association will be among Jennifer's top priorities. Her telephone number is 202-261-6531.

STABLE TIMES
First Quarter 2000
Stable Times is a benefit of SVIA membership.
Published by the Stable Value Investment Association located at 2121 K Street, NW; Suite 800, Washington, DC 20037; phone 202-261-6530; fax 202-261-6527; and www.stablevalue.org.

Sell High, Buy Low *continued from page1*

Further participants do not respond to market volatility (Table 3). For example, on August 31, 1998 only 0.46% of participants changed in their balance allocations. This is the day when the DOW dropped 513 points, its biggest one-day loss of the year, and 1 billion shares were traded for the first time on the New York Stock Exchange. Fidelity Investments concluded that "there is no predictable relationship between increases and decreases in (fund) exchanges and increases and decreases in the DOW."

Table 1
Percent of participants holding different numbers of investment options in 1998

Options	Percent Holding
1	25%
2	20%
3	19%
4	14%
5 or more	22%

Building Futures: *How American Companies Are Helping Their Employees Retire—A Report on Defined Contribution Plans, Fidelity Investments, 1999.*

It is good that throughout the stock market volatility of the past several months, plan participants have, for the most part, stayed the course, not reallocating their 401(k) assets, embracing an "in it for the long haul" ideology and avoiding attempts to market time. However, being too passive also has negative consequences. The problem is not that participants have traded too much in their accounts, it is that they have traded too little.

If participants do not periodically rebalance the assets back to their original allocation percentages they risk having markets make the allocation for them. This is because without periodic rebalancing, the better performing asset classes will become a greater portion of the overall portfolio over time. For example, equities have substantially outperformed fixed investments like stable value and money market funds since 1990. The lack of rebalancing is one of the reasons that the investment of defined contribution assets has changed so dramatically since 1990 (Table 4).

Table 2
Fund Exchange Behavior By Participant Age in 1998

Age	Percent Who Made No Change
10-29	88%
30-39	81%
40-49	77%
50-59	72%
60-64	73%
65-69	76%

Same Source as Table 1

Table 3
Participant Exchanges on the Ten More Volatile Days for the DOW in 1998

Date	DOW Change From Previous Day	Percent of Participants Making An Exchange
August 31	-6.40%	0.46%
August 27	-4.20%	0.30%
August 4	-3.40%	0.29%
September 10	-3.20%	0.19%
September 30	-2.90%	0.64%
January 9	-2.80%	0.25%
September 8	+5.00%	0.26%
October 15	+4.10%	0.19%
September 1	+3.80%	0.60%
September 23	+3.30%	0.17%

Same Source as Table 1

In addition to helping participants stay in control of their portfolios, periodic rebalancing has the additional benefit of forcing participants to sell high and buy low. That's because at the point when rebalancing occurs the best performing asset is sold and the worst performing is bought.

Billions of dollars and millions of hours have been invested by plan sponsors and service providers teaching participants about types of investments and the value of long term investing. Now it is time to put rebalancing on our plan education agenda.

Table 4
1990–1998 DC Investment Allocation

Equity Funds	45%	74%
GIC/ Stable Value Funds	28%	10%
Cash/Money Market	11%	3%
Other	16%	3%

PSCA's 34th and 42nd Annual Surveys of Profit Sharing and 401(k) Plans

David L. Wray *is the president of the Profit Sharing /401(k) Council of America (PSCA), a national, non-profit association of companies that sponsor profit-sharing and 401(k) plans for over 3 million employees. He is a nationally recognized authority on defined-contribution plan issues. Wray also is executive director of the Profit Sharing/401(k) Education Foundation (PSEF), a non-profit educational organization dedicated to disseminating facts about the most effective uses of profit-sharing, 401(k), and related plans.*

Highlights from the 1999 Stable Value Fund Investment and Policy Survey

Interest Rate Risk Management Differences by Manager Segment

By Judy Markland, Landmark Strategies

The Association's annual stable value fund investment survey provides a unique window on the differences in SV management styles by manager segments of the market. Four market segments were surveyed: in-house and external managers of individual funds, commingled pools managed by investment firms and banks, and commingled funds managed by life companies for their bundled or full-service defined contribution business. Each segment provides SV funds that offer principal stability along with high, relatively stable yields that track market interest rates reasonably well. Interestingly, the approaches that they take to achieve this result vary - especially when it comes to the management of interest rate risk within the fund.

Rising interest rates pose two potential problems for a stable value fund. The first is that the fund's blended rate credited to participants may lag the upturn in market rates, making the fund less attractive for new contributions and perhaps stimulating outflows. The second is a potential for market losses on participant withdrawals on contracts with participating wraps. Although any such losses are amortized through the wrap guarantee and reflected as a small deduction in the credited rate, they depress the blended rate and worsen the lag problem. Falling interest rates have the opposite effect on a SV fund - blended rates higher than market rates and potential market gains on participant withdrawals.

Factors Affecting Interest Rate Risk Exposure in SV Funds
Data as of 12/31/98

	Individually Managed		Commingled	
	External Mgmt.	In-house Mgmt.	Bank and Invest. Co. Pools	Life Co. Full Service
fund duration (yrs.)	2.3	3.2	2.4	3.7
% of fund in cash	7.6%	3.7%	8.4%	0.4%
% of fund in participating contracts	68.3%	26.0%	59.7%	82.3%

The longer the duration of the stable value fund, the greater the potential blended rate lag and size of any gains or losses realized on participating contracts. Managing interest rate risk is one of the major responsibilities of a stable value fund manager.

As the attached table illustrates, in-house and full-service managers have opted for fund durations of 3.2 and 3.7 years respectively - 8 to 14 months longer than the two other manager segments. One reason for the longer duration is the smaller cash position in their funds. In-house managers have only about 4 percent in cash and full-service managers less than 0.5% on average.

Both segments have opted for the extra yield that comes on average with a slightly longer duration and believe that its benefit outweighs any increased risk of rate lag. This really shouldn't be surprising, since rate lag isn't as much of a problem for them. In-house managers are less vulnerable to being replaced in an underperforming period than an external manager. Many full service funds credit a current or "new money" rate on new deposits and new sales rather than the aggregate portfolio rate.

External individual fund managers and pool managers, on the other hand, have lower fund durations (2.3 and 2.4 years respectively), partly as a result of the larger cash positions in their funds. The shorter duration helps keep the blended rate more current, important when it is the yield credited to new plans in the fund, as is the case with the pools.

Both the external manager and pool segments also use cash as the first layer after contract maturities to pay benefit payments. The cash buffer helps reduce withdrawal risk charges, which helps offset some of the cost of holding the cash. Greater reliance on participating contracts by both segments enhances yield via lower risk charges. With the shorter fund durations, there is less risk that rising rates will result in market losses on withdrawal activity under these par contracts.

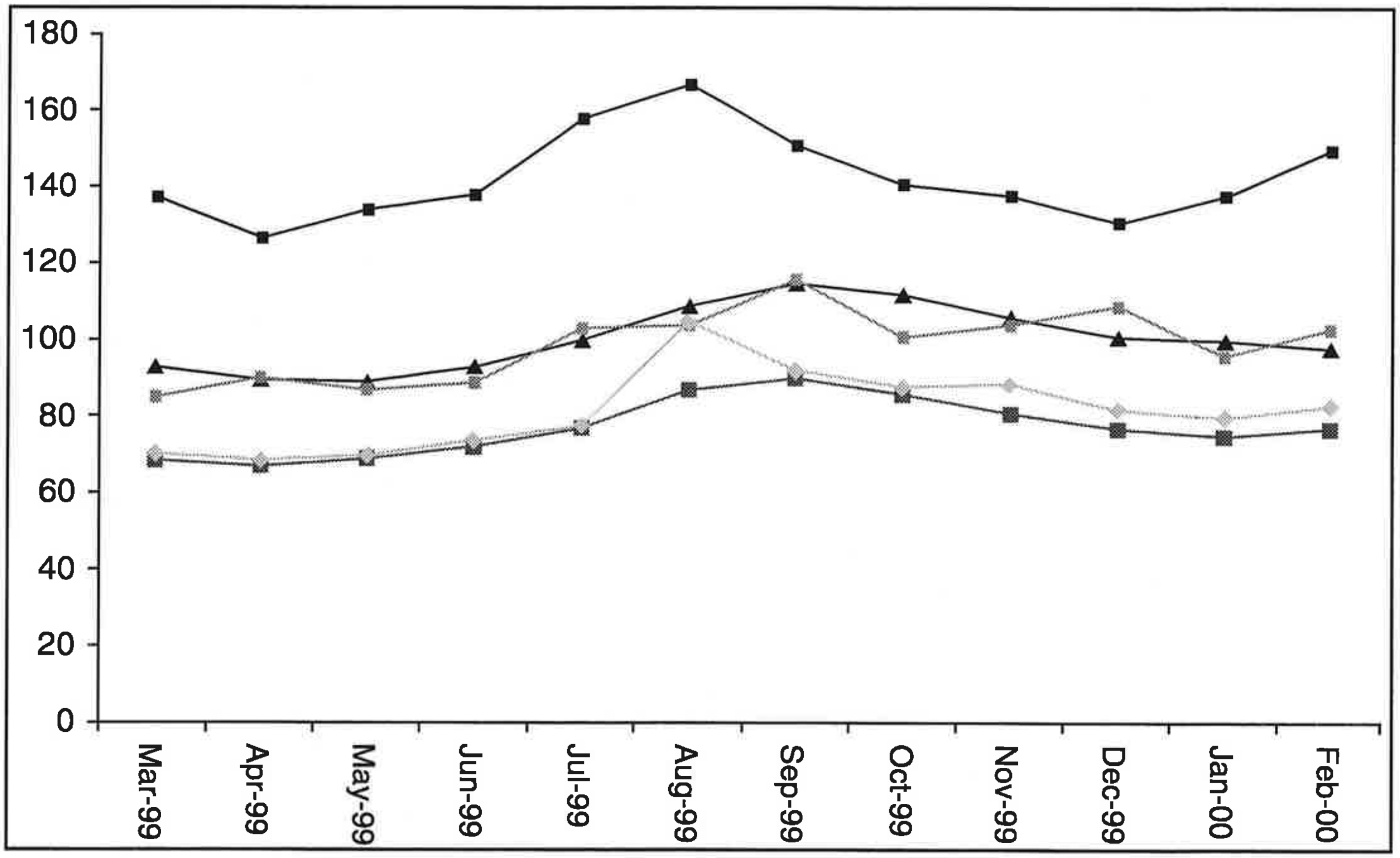
Given all this, it may seem puzzling that full-service managers - the segment with the highest overall duration - also have the highest percentage of participating contracts. This is partially explained by the fact that 39% of the segment surveyed use the class-year or pro-rata by participant withdrawal protocol, in which participants' yields are generally affected only by their own contribution and withdrawal activity. There is little risk of one participant's actions influencing another's yield with this withdrawal protocol.

Clearly, there's far more than one way to 'skin a cat' when it comes to stable value fund investing. The SVIA survey provides some useful insight into the differences in style and portfolio structures utilized in the industry.

Tracking Stable Value Yield Spreads, March 1999 to February 2000

By Karl Tourville, Galliard Capital

Interest rates have continued their upward climb during the last several months on the short end of the curve as strong economic growth coupled with modest inflation has lead the Federal Reserve to maintain a tightening bias. The long end of the curve has inverted with the 30 Yr. Treasury yielding 6.15% as of 2/29, which is lower than the 1 Yr. yield of 6.23%. This inversion is a result of the reduced supply of longer-term Treasury securities as the US Treasury cuts back issuance and buys back debt. In this environment there has been an upward pressure on spreads particularly in the mortgage-backed sector. GIC spreads have remained constant over past few months with the 5 Yr. GIC spread at approximately 100 over Treasuries.



Fourth Quarter 1999 STABLE TIMES Crossword Puzzle Answers

A	L	L	O	C	A	T	E		P	R	E	M	I	U	M
N		U		O			S		O		N		M		O
A	S	S	U	M	E		C	A	L		M		P	E	N
L		T		E			H		I		I		A		O
Y	I	E	L	D		M	E		T	I	T	H	I	N	G
S		R		Y	E	O	W		I		Y		R		O
I			F			D			C			U			M
S	A	T	I	A	T	E	D		S	C	A	D	U	T	O
	S	E	A	L			E			A		O			U
P	A	R	T	I	C	I	P	A	N	T		N	O	U	S
A		M			M		L						W		
S	P	I	L	L	O	V	E	R		R	O	L	L	U	P
S		N					T	A	C	O		E			R
I	S	A	B	E	L		I	M	E	L	D	A		P	I
V		T		S	A	C	O		T	E		S			M
E	L	E	C	T	I	O	N		E	X	P	E	N	S	E

Mark Your Calendar!

The SVIA 2000 National Forum is scheduled for October 10-12, 2000 at the Monarch Hotel in Washington, D.C.

A Better Solution for the Reluctant Investor

By Michael S. Falk, Strategic Financial Concepts, Inc.

GUEST OPINION

The 401(k) has become somewhat of a ubiquitous employee benefit. Not only is the 401(k) available to most everyone, but it is also a benefit to all that take advantage of it. Unfortunately, the benefit could be greater. In terms of investment performance, the industry has seen that the individual asset allocation decisions have been poor. A study by Watson Wyatt has shown the average performance of 401(k) plans has underperformed defined benefit plans by 200 basis points per year. Perhaps the solution exists in the basic acknowledgement that not all 401(k) participants, in general, do not know how to, do not want to, or don't have the time to invest properly. These are the participants we refer to as the "reluctant investors." Not all individuals are motivated investors. Many are reluctant, and no amount of education is going to change that.

There is little doubt that the underperformance is due to a lack of investment knowledge and training by the average participant. There are many attempts at providing solutions in an effort to improve upon participant investment allocations. Those attempts have fallen mainly into three categories:

- **EDUCATION/COMMUNICATIONS**
- **LIFESTYLE FUNDS**
- **INVESTMENT ADVICE**

While education and communications are listed under the same heading, they are very different. The rationale for including them together is due to their common logistical problems. The issues here surround getting the right (or needed) information to the participant that would benefit from it in a way that will result in improved behavior. The hurdles experienced en route to the improved behavior are many. The first and perhaps biggest hurdle is the apparent fact that people rarely read materials/information that is provided to them. This can be due to language issues, reading skills, the inability to understand what is written, lack of time, lack of interest and so on. If we consider this conundrum in terms of adult learning constructs, then the difficulties may be due to the delivery method. Many participants may learn better with the advent of seminars and workshops. The issues of cost and attendance logistics (i.e. locations and shift times) complicate these alternatives. It has been noted by many industry studies that participants in 401(k) plans are in need of more education and assistance.

One seemingly simple attempt at providing a solution or rather assistance to the 401(k) participant was the introduction of "lifestyle" funds. When properly understood and used, the offering of these funds narrows a participant's investment allocation decision to one question, what percentage allocation to equities do I need? While this is a solid attempt at providing assistance in a simple manner, there are two resulting dilemma's: participants are using more than one "lifestyle" fund, and the critical question regarding the equity allocation is still unanswered. The results also show minimal usage of these funds by participants. Perhaps the usage is low because "lifestyle" funds do not have long and strong enough track records to attract interest in a market producing 20% returns every year. Understand that these funds are at best a potential panacea. "Lifestyles" often have fees levied beyond the underlying management fees, managerial construction issues such as only one fund family's talent, and finally the usage of bond funds in lieu of the better risk/return diversifier, stable value.

Lately, advice has drawn a lot of attention. What many participants desire is someone to perform the portfolio design and management for them. An interesting question would be, isn't that what many participants always wanted. In fact, a survey done by Buck, KPMG, and Access Research said that 20% of participants are already using a financial planner for advice on their account. The current direction of the industry is providing advice to participants over the Internet due to the dramatic efficiencies in implementation and costs, the democratization of investment advice. While this appears to be a solution to the participant, it is not that simple. Consider those reluctant investors identified above - they do not know how to, do not want to, or don't have the time to invest properly. Do they sound like the type of individual that would go through the following process:

1. Get on the Internet - is access universally available?
2. Answer questions regarding assets, goals, and risk tolerance - are the responses dependable, are the questions understood, do the questions induce bias, do the questions assume a certain level of knowledge...?
3. Receive advice and follow it - could the advice be ignored?
4. Redo whenever there is a significant change in one's life or at a minimum every couple of years - good advice today may not be good advice tomorrow.

The "reluctant" investor participant would either not undertake the effort, or at a minimum skip step number four, which would completely invalidate this potential solution. While the net is a viable solution, its long-term results are in question, and it caters to a more motivated individual. And aren't motivated participants more likely to be accepting of education and communication efforts?

DEALING WITH INERTIA — A BETTER SOLUTION

Since there are always some participants who are not willing or able to make knowledgeable investment decisions, then why not have an

A Better Solution *continued on page 7*

A Better Solution *continued from page 6*

advisor available to perform the portfolio design and ongoing management, and why not make that an option in the plan. In addition, why not take the next step and make it the default option so that those participants that do nothing receive professional portfolio management. The motivated participants can simply opt out to the plan's investment choices, or even a brokerage window if available.

There are a few plans that have already adopted this approach. For participants who so elect, the advisor performs the asset allocation decisions based upon the participant's time horizon and integration with other employer sponsored retirement benefits. Once the asset allocation is determined, the money is invested and the resulting mix is reviewed annually with rebalancing performed at least that often. The existing plan options would generally be used and the advisory fees would be paid either by the participant or the plan sponsor. A knowledgeable advisor will have the flexibility to use stable value instead of bonds in the asset allocation process, an advantage usually not available to lifestyle fund investors.

There is no requirement for participant-entered data, and therefore less chance for error due to faulty information, or simply information that changes frequently and substantially. While the asset allocation decisions may be less tailored to the individual as a result, this will in all likelihood result in decisions far superior than the having the reluctant investor do her own "analysis." This approach also keeps advisory fees very reasonable.

It is recommend that those with substantial "outside" retirement-dedicated assets opt out and make their own investment choices. A study by Vanguard in 1996 showed that approximately two-thirds of all participants have relatively few assets outside of their employer-sponsored retirement plans. Even for those individuals that have "outside" assets, are they dedicated to retirement? It is also suggested that spousal assets not be considered because of their uncertain nature in an environment where the national divorce rate exceeds 50%.

A large segment of DC investors are unwilling or unable to make intelligent investment decisions and for them, programs such as education, lifestyle funds and advice on the Internet will not make much of a difference. For this segment, an advisory service which requires little or no effort by the investor, yet provides professional asset allocation and management, will result in better investment decisions and a greater comfort level by both the participant and the plan sponsor.

***Stable Times would like to thank Mr. Falk for this article and encourage readers with different points of view to submit articles for publication in future newsletters.*

Michael Falk *is a director of Strategic Financial Concepts, specializing in investment analysis and portfolio design. He has over ten years of experience in DC investment and education consulting. SFC provides consulting/investment services to defined contribution plans, defined benefit plans, healthcare organizations and not-for-profit institutions. The advice product discussed in this article, SFCPROgram, was first launched 1999. Michael was instrumental in its design and in the implementation work for the first SFCPROgram client, SwedishAmerican Health Systems.*

Performance Measurement Task Force Update *continued from page 1*

has always been possible with wrapped bond portfolios with no concern about whether the book value accounting on those assets is in jeopardy. Plan sponsors can ensure that a manager's objectives do not stray from those of the participant during the fund design process, which includes tailoring benchmarks and investment guidelines to participant objectives.

AIMR Endorsement of our methodology is a clear objective. AIMR involvement will help ensure the legitimacy of our methodologies and support stable value as a credible vehicle for the long term. We will present our final conclusions to the new AIMR IPC Committee for comment and inclusion along all other asset categories addressed in AIMR's Performance Presentation Standards. In addition, it is believed that it is quite possible for managers to comply with AIMR PPS standards today. This requires marking GICs to market and applying all other AIMR standards for stable value assets. The final outcome of the task force will be an adoption of AIMR-PPS with noted exceptions and additions to reflect the unique aspects of stable value assets. The task force will not reproduce standards and language of AIMR that is applicable to all asset classes. Our document alongside the existing AIMR-PPS materials will be a complete guide to general performance measurement standards. This document will be distributed within the industry and AIMR IPC for review. We will enhance this document with more detailed "how to" articles to be published in Stable Times.

OPEN ISSUES REMAIN

There is no controversy about whether to value traditional GICs, but rather, we are still addressing to what degree the task force should provide detailed methodology. A majority of respondents prefer disseminating detailed information about how to value GIC portfolios. Some even favor creation of rules. Others feel that this is beyond the scope of the project, because AIMR does not typically take a prescriptive approach and most financial professionals can figure out an approach that is reasonable and consistent. Likewise, methodology for valuing the benefit responsive insurance component GICs and wraps has been subject to extensive technical debate by task force members. You can expect to see specific 'how to' steps distributed for this unique aspect of stable value asset valuation.

Effective dates are tricky. Not everyone can start as of 1/1/2000 with an AIMR-compliant performance reporting system. Re-creation of past history is a heavy burden. We will probably start off as up to each manager to decide their chosen strategy, but AIMR may proclaim an effective date requirement or an acceptable time frame for relief.

There was discussion about establishing a centralized resource for performance measurement issues. There will inevitably be questions from managers and plan sponsors. Guidance on gray areas may be necessary. Mediation of disputes could become an issue. Most task force members favor a role for SVIA but the specifics are unclear. On the other hand, in other industries, there exists no such centralized resource and standards ultimately develop naturally.

Appropriate disclosures is a big topic that is the center of the most active discussion today. In general, the task force will present required disclosures that are most significant for fair and accurate presentation of performance results. We will also provide guidance on recommended disclosures that are particularly relevant to stable value funds.

DOL PUBLISHES ERISA §401(C) REGULATION

Protection from Fiduciary Liability for Certain Insurance Contracts

By Al Turco, Pepe & Hazard

On January 5, 2000, the Department of Labor ("DOL") issued a final regulation pursuant to ERISA §401(c), which regulates the terms of certain insurance contracts issued to ERISA employee benefit plans that are backed by an insurer's general account assets (See 65 Fed. Reg. 639 (January 5, 2000)). The regulation is intended to provide a "safe harbor" from certain types of ERISA liability for insurers that issued insurance contracts, particularly group annuity contracts, before January 1, 1999, ("Transition Policies"). While the regulation will likely affect the conduct of insurers, employers and stable value funds that hold Transition Policies will also have an interest in its implementation.

BACKGROUND

Under ERISA §401(b)(2), if an insurer issues a "guaranteed benefit policy" to a plan, the assets of the plan are deemed to include the policy, but do not, solely by reason of the issuance of the policy, include any assets of the insurer. In 1993, the Supreme Court held in John Hancock Mutual Life Ins. Co. v. Harris Trust & Savings Bank, 510 U.S. 86 (1993), that the "unallocated portion" of a John Hancock group annuity contract did not constitute a guaranteed benefit policy. Consequently, assets attributable to the unallocated funds were plan assets for purposes of ERISA's fiduciary and prohibited transaction rules.

The Harris Trust decision did not provide detailed guidance as to what types of insurance policies and what specific policy features would be considered guaranteed benefit policies. As a result, insurers, plan fiduciaries, and investors have been unable to reliably determine when contracts issued to ERISA plans could result in the application of ERISA's fiduciary and prohibited transaction rules to the management and operation of insurance company general account assets.

As a result, in the Small Business Job Protection Act of 1996, Congress established ERISA §401(c), which grants insurers retroactive relief from the application of ERISA's fiduciary and prohibited transaction rules for Transition Policies. ERISA §401(c) required the DOL to issue regulations to extend this protection to insurers. Prospectively, Transition Policies will remain protected and "plan assets" will not be created within an insurer's general account, if the insurer complies with the conditions of the final regulation.

THE REGULATION

The Regulation includes a prudence standard applicable to the management of general account assets and a requirement that policies be purchased by persons independent of the insurer. The regulation also requires a number of disclosures, the provision of certain minimum termination rights and protection from insurer-initiated amendments. These latter requirements, which must be satisfied if the insurer is to avail itself of the "safe harbor" protection, are summarized below.

DISCLOSURE

An insurer must provide significant disclosure with respect to each Transition Policy, both initially and annually.

A. Initial Disclosure. Given that all Transition Policies have been issued, initial disclosure is required to be provided to each policyholder by July 5, 2000. Generally, the content of the initial disclosure is to include:

(1) A description of the method used to determine the fees, charges or expenses that are, or may be, assessed against the policyholder, including the extent and frequency with which Transition Policy fees may be modified.
(2) A description of the method used to determine the return to be credited under the Transition Policy, including the allocation of income and expenses within and among lines of business and business segments.
(3) A description of the rights which the policyholder or plan participants have to terminate contributions or to make withdrawals under the Transition Policy and a description of any fees, credits, market value adjustments, both positive and negative, that may apply to a withdrawal.
(4) Within 30 days of a policyholder request, the formula actually used to calculate the Transition Policy's market value adjustment, if any, a description of the component parts of any formula and, a market value calculation.
(5) A statement describing the expense, income and benefit guarantees under the Transition Policy, including the insurer's right, if any, to modify or eliminate these guarantees.

B. Annual Disclosure. Annually, beginning after January 5, 2000, but not later than July 5, 2001, the insurer must provide additional disclosure to each policyholder. Generally, the content of the disclosure for each annual reporting period is to include:
(1) The opening and closing Transition Policy balance, deposits, an itemized income statement, the crediting rate (gross or net), an itemized expense statement, an accounting of benefits paid, annuities purchased, withdrawals made and other transactions affecting the Transition Policy balance.
(2) An estimate of the termination value of the Transition Policy as of the end of each annual disclosure period.
(3) An explanation that the insurer will make available, upon request, copies of publicly available financial data or other publicly available reports relating to the financial condition of the insurer.

DOL Publishes ERISA Regulations *continued on page 9*

DOL Publishes ERISA Regulations *continued from page 8*

TERMINATION PROCEDURES

By July 5, 2001, an insurer must permit each policyholder to terminate a Transition Policy, upon providing ninety days notice, including the right to elect either of two required distribution options for payment of unallocated amounts.

(1) The first distribution option provides for a lump sum payment to the policyholder of all unallocated amounts. The insurer may apply a "two-way" market value adjustment to the lump sum payment, and may recover costs actually incurred by the insurer that would otherwise have been recovered but for termination of the Transition Policy.
(2) The second distribution option allows the policyholder to receive a book value payment of unallocated amounts in approximately equal annual installments over a period of no longer than ten years. Under this option, interest on the remaining Transition Policy balance must be credited at a rate no less than the annual rate credited as of the date of termination, minus one percent.

INSURER-INITIATED AMENDMENT

Effective immediately, an insurer must provide written notice to each policyholder at least 60 days prior to the effective date of any insurer-initiated amendment. An insurer-initiated amendment includes:

(1) An amendment to a Transition Policy made by the insurer pursuant to a unilateral right to amend the Transition Policy terms that would have a material adverse effect on the policyholder.
(2) Certain changes in the insurer's conduct or practice that has more than a "de minimus" adverse effect, including:

(i) A change in methodology for assessing fees or for allocating income or expenses within and among lines of business or business segments or for determining the rate of return under the Transition Policy.
(ii) A change in the policyholder's rights or in the insurers' methods or practices applicable to the termination of the Transition Policy, withdrawal of funds, or the purchase of annuities for plan participants.

CONCLUSION

Compliance with the regulation by an insurer will, in many instances, likely involve development of disclosure material and the preparation of a "compliance amendment". In some instances, an insurer may conclude that a policy (or class of policies) it has issued, is an ERISA guaranteed benefit policy for which a "safe harbor" is not needed. Should the insurer later discover that the policy is not a guaranteed benefit policy or should a Transition Policy not be in compliance, the regulation provides a remediation process, intended to insulate the insurer from ERISA fiduciary liability and to forestall plan asset status for assets held in the insurer's general account for a limited period.

For the employer or stable value fund that holds a Transition Policy, now may be an appropriate time to audit the contract or to arrange a restructuring of its terms with the insurer.

Polish Delegation Visits SVIA

Government officials charged with privatizing Poland's pension program paid a visit to SVIA headquarters in Washington, DC last week to learn more about the Stable Value option from John Hancock's Wayne Gates, SVIA Board Member and Co-Chair of the Data and Research Committee, and Gina Mitchell, SVIA President.

The twelve-member group was made up of officials from the Poland pension fund regulator, Urza Nadzoru nad Funduszami Emerytalnymi, (UNFE). The UNFE officials stopped in Washington as part of a larger study tour arranged by Pricewaterhouse Coopers. The tour was designed to enhance UNFE's institutional capacity to supervise the voluntary employee pension plans by broadening the knowledge and networks of its key staff.

Wayne and Gina began the meeting with an informative presentation on the benefits of Stable Value. The group was particularly interested in SVIA's efforts to educate plan sponsors and the general public. Their concerns included market volatility, specifically the chance that an investor might lose everything, and how to ensure voluntary participation by plan sponsors and employees.

SVIA is honored to have been included in UNFE's study tour. The Association's efforts are being noticed, and that is a tribute to every member. Clearly, interest in Stable Value is growing worldwide.

401(k) Investing — A Look At The Data

By Dallas Salisbury, EBRI

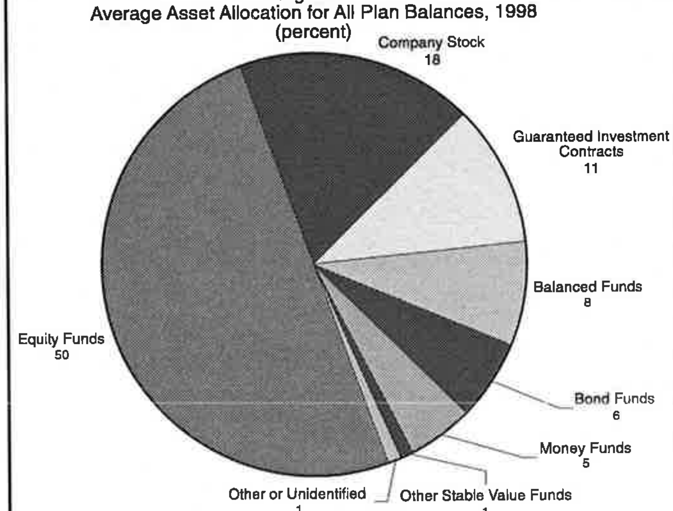
As 401(k) retirement plans have grown to be a significant part of the private pension landscape in the United States, interest in examining the behavior of 401(k) plan participants also has grown. The project has now collected data for year-end 1997 and year-end 1998. The purpose of this article is to report findings from the year-end 1998 data. [1] The 1998 EBRI/ICI database accounts for 11 percent of all 401(k) plans, 22 percent of all 401(k) participants, and about 27 percent of the assets held in 401(k) plans.

FINDINGS

This analysis of the 1998 data updates the analysis of the 1996 data and reports on 401(k) participant asset allocation, participant account balances, and loan activity. The results for year-end 1998 are broadly similar to those for year-end 1996. In addition, this analysis presents data regarding asset allocation by plan size and examines the changes in the accounts of certain participants who were included in the 1996, 1997, and 1998 studies.

- For all 401(k) participants in the 1998 EBRI/ICI database, almost three-quarters of plan balances are invested directly or indirectly in equity securities. Specifically, 49.8 percent of total plan balances are invested in equity funds, 17.7 percent in company stock, 11.4 percent in guaranteed investment contracts (GICs), 8.4 percent in balanced funds, 6.1 percent in bond funds, 4.7 percent in money funds, and 0.3 percent in other stable value funds.
- The asset allocation of participants' account balances varies with age. Younger participants' assets tend to be more concentrated in equity fund investments, while older participants invest more heavily in fixed-income assets.

Figure 1
Average Asset Allocation for All Plan Balances, 1998
(percent)



Source: Tabulations from EBRI/ICI Participant-Directed Retirement Plan Data Collection Project

Footnotes

1 Summary figures for year-end 1997 are available at ICI's Web site at www.ici.org/pdf/per06-01_appendix.pdf. Hardcopy may be requested by calling ICI's Research Department. The 1997 EBRI/ICI database contains 29,899 401(k) plans with $290 billion of assets and 7,056,418 active participants.

- Investment options offered by 401(k) plan sponsors influence participants' asset allocation. Plans offering the basic investment options of equity, balanced, bond, and money funds tend to have the highest allocations to equity funds. The addition of GICs to the four basic investment options reduces the relative allocations to all other investment options, particularly bond funds and money funds. Alternatively, the addition of company stock to these options substantially reduces the allocation to equity funds and balanced funds.
- Asset allocation does not vary significantly across plan size for plans offering the basic investment options of equity, balanced, bond, and money funds. When GICs, company stock, or both, are added to the basic options, asset allocation varies with plan size.
- Employer contributions in the form of company stock affect participants' asset allocation behavior. Participants in plans in which the employer contribution is required to be invested in company stock have a higher percentage of their self-directed account balances in company stock and lower percentages invested in equity funds and balanced funds, compared with participants in plans with no employer-directed contributions.
- The allocation of plan balances to equity funds varies across participants. Indeed, about 28 percent of participants have more than 80 percent of their account balances invested in equity funds, while about 28 percent hold no equity funds at all. However, about two-thirds of those participants with no equity funds have exposure to equity securities through balanced funds or company stock. As a result, overall equity-related investments of those holding no equity funds are 44.6 percent of plan balances.
- Asset allocation varies with participant salary. In particular, the percentage of account balance invested in equity funds rises with salary, while the percentage invested in GICs declines as salary rises.

ACCOUNT BALANCES

- The average account balance (net of plan loans) for all participants was $47,004 at year-end 1998, which is 26 percent higher than the average account balance at year-end 1996. The median account balance was $13,038 at year-end 1998. The reported account balance represents retirement assets in the 401(k) plan at the participant's current employer. Retirement savings held in plans at previous employers or rolled over into individual retirement accounts (IRAs) are not included in this analysis.

401(k) Investing *continued on next page*

401(k) Investing continued from previous page

Figure 2

Average Asset Allocation by Age and Investment Options, 1998

(percent of account balances)

	Equity Funds	Balanced Funds	Bond Funds	Money Funds	Guaranteed Investment Contracts	Company Stock
ALL AGES COMBINED Investment Options						
Equity, Bond, Money & Balanced Funds	66.4	13.0	9.8	8.4		
Equity, Bond, Money & Balanced Funds& GICs	58.2	10.0	4.7	4.0	20.9	
Equity, Bond, Money & Balanced Funds & Company Stock	40.7	5.8	11.5	6.7		32.7
Equity, Bond, Money & Balanced Funds, & GICs & Company Stock	44.4	7.1	2.1	2.3	18.7	24.3
PLANS WITH NO COMPANY STOCK OR GUARANTEED INVESTMENT CONTRACTS						
Age						
20s	74.3	10.0	7.6	6.0		
30s	73.3	11.5	7.6	5.9		
40s	69.0	12.7	8.9	7.2		
50s	63.4	14.0	10.5	9.0		
60s	52.7	15.1	15.4	13.8		
PLANS WITH GUARANTEED INVESTMENT CONTRACTS						
20s	70.7	8.4	3.6	3.5	11.3	
30s	68.7	8.8	3.9	3.1	13.2	
40s	62.5	9.7	4.4	3.8	17.4	
50s	55.6	10.5	5.1	4.0	22.7	
60s	41.9	10.0	5.8	4.9	35.8	
PLANS WITH COMPANY STOCK						
20s	47.4	6.0	5.9	6.4	32.5	
30s	47.4	6.1	6.8	6.0	32.2	
40s	44.0	6.2	8.7	6.8	32.6	
50s	38.4	5.7	12.5	6.8	33.7	
60s	31.0	5.1	20.7	7.1	31.7	
PLANS WITH COMPANY STOCK AND GUARANTEED INVESTMENT CONTRACTS						
20s	53.1	7.7	1.7	2.1	7.9	25.2
30s	49.5	7.2	1.7	1.8	9.7	28.5
40s	45.4	7.2	2.0	2.1	13.7	28.2
50s	44.9	7.3	2.3	2.3	19.3	22.9
60s	39.5	6.9	2.3	2.9	31.6	16.0

- Almost one-half of participants have account balances of less than $10,000 in the 401(k) plan at the participant's current employer, while 13 percent have balances greater than $100,000. Those individuals with account balances of less than $10,000 are primarily young workers or workers with short tenure at their current employer. In contrast, those with account balances in excess of $100,000 are primarily older workers or workers with long tenure, who have accumulated larger account balances through years of contributions and the compounding of investment returns.
- The ratio of account balance to 1998 salary varies with salary, increasing slightly as earnings rise from $20,001 to $80,000, and falling a bit for salaries greater than $80,000. The increase in ratio likely reflects a greater propensity of higher-income participants to save, whereas the decline after $80,000 results from contribution and nondiscrimination rule constraints.
- The ratio of account balance to 1998 salary varies with age and tenure. Older participants, who have had more time to accumulate

401(k) Investing *continued on next page*

401(k) Investing *continued from previous page*

balances, have higher ratios than younger participants. Similarly, within a given age group, participants with more years of tenure have higher ratios than those with less tenure.

PLAN LOANS

- Fifty-six percent of the plans, accounting for 80 percent of the participants, offer loans to plan participants. The probability of a plan sponsor offering plan loans to its employees increases with plan size. Indeed, about 90 percent of plans with more than 10,000 participants offer a loan provision, while less than half of plans with 10 or fewer participants do so.
- Among participants eligible for loans, 16 percent had outstanding loans at the end of 1998. Loan activity varies with age, tenure, and account balance. Participants between age 30 and 59 are more likely to borrow than older or younger workers. Similarly, individuals with short or long periods of tenure are less likely than other participants to have a loan outstanding. Finally, participants with account balances of less than $10,000 tend to borrow less frequently.
- For those with outstanding loans at the end of 1998, the level of the unpaid balance represents 14 percent of the account balance, net of the unpaid loan balance.

PARTICIPANTS' ACCOUNTS, 1996-1998

- Approximately 3.3 million (or 50.3 percent) of the participants present in the 1996 EBRI/ICI database also are in the 1997 and 1998 EBRI/ICI databases. Three-quarters of these participants generally held about the same percentage of equity securities in year-end 1996 and year-end 1998.
- The median growth in account balance between 1996 and 1998 was 86 percent among all participants present in 1996, 1997, and 1998, in part reflecting strong stock market performance. For a given age group, median account growth (measured in percentage terms) tends to fall as tenure increases, primarily because initial account balance rises with tenure. Within any given tenure range, younger participants experience a higher percentage median account growth than older participants, in part because of their higher exposure to equity securities.

Figure 3

Impact of Company Stock on Asset Allocation by Age, 1998

(percent of account balances)

Age Cohort	Equity Funds	Balanced Funds	Bond Funds	Money Funds	Guaranteed Investment Contracts	Company Stock
PLANS WITH EMPLOYER-DIRECTED AND PARTICIPANT-DIRECTED BALANCES						
Total Balances (Employer-Directed and Participant-Directed)						
20s	36.1	5.5	0.7	1.9	6.8	48.9
30s	32.0	5.0	0.7	1.7	7.3	53.1
40s	26.8	5.4	1.2	3.3	7.8	55.2
50s	25.2	6.1	1.7	4.2	10.4	52.1
60s	23.6	6.7	3.1	7.5	17.4	41.6
All	26.7	5.7	1.6	3.9	10.0	51.9
Participant-Directed Balances Only						
20s	49.4	7.5	0.9	2.5	9.3	30.3
30s	46.9	7.3	1.0	2.4	10.7	31.5
40s	40.1	7.9	1.8	4.8	11.8	33.2
50s	36.0	8.5	2.5	6.1	14.2	32.3
60s	30.1	8.4	4.0	9.7	21.4	26.1
All	38.3	8.1	2.3	5.5	14.0	31.5
PLANS WITH COMPANY STOCK INVESTMENT OPTION BUT NO EMPLOYER DIRECTED CONTRIBUTIONS						
Total Balances						
20s	51.5	10.5	2.2	6.5	5.3	19.1
30s	49.4	10.1	2.5	5.3	6.4	23.2
40s	44.7	10.4	3.1	5.6	8.9	24.4
50s	40.0	11.4	3.9	6.5	12.5	23.3
60s	30.8	11.5	4.6	9.1	20.1	21.6
All	42.2	10.8	3.4	6.4	11.1	23.4

Note: Minor investment in other stable value funds and "other" are not shown; therefore, row percentages will not add to 100 percent. Employer-directed balances are instock.

401(k) Investing *continued on next page*

401(k) Investing *continued from previous page*

Figure 4

Asset Allocation Distribution for Participants with No Equity Fund Balances by Age and Tenure,

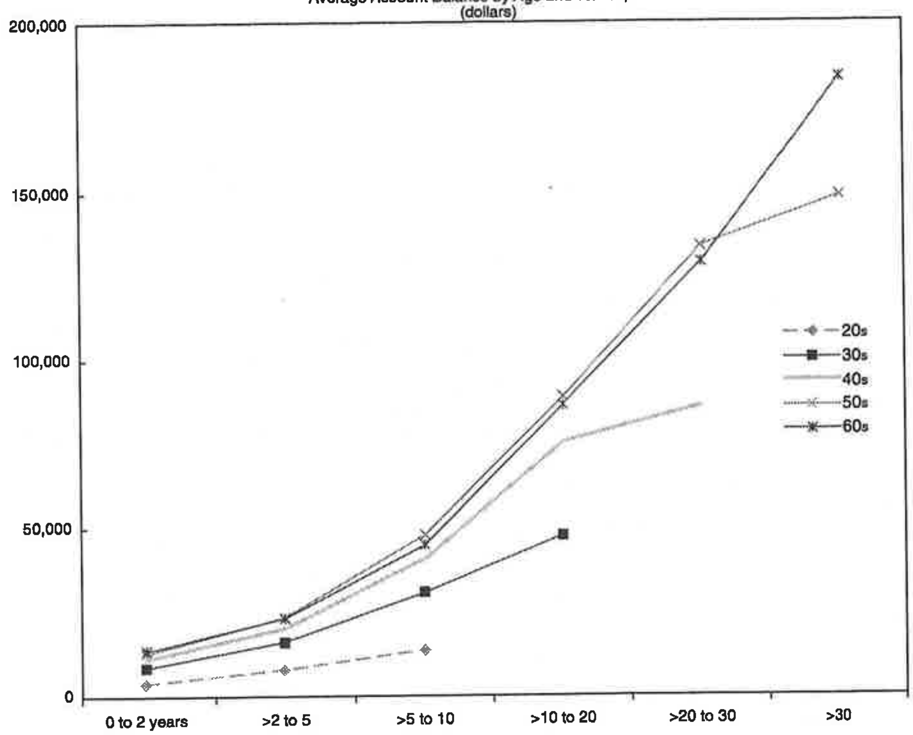
(percent of account balances)

	Balanced Funds	Bond Funds	Money Funds	Guaranteed Investmen Contracts	Other Company Stock	Stable Value Fund	Other	Unknown	Total
AGE COHORT									
20s	3.1	8.6	17.4	15.3	40.1	0.6	3.9	1.1	100.0
30	11.1	8.1	13.2	16.2	47.6	0.3	2.5	1.1	100.0
40s	10.0	8.3	11.9	20.7	45.4	0.4	2.0	1.3	100.0
50s	9.5	9.5	10.6	25.9	40.4	1.2	1.5	1.5	100.0
60s	8.4	12.7	10.4	37.8	26.6	1.7	1.3	1.1	100.0
All	9.5	9.8	11.4	26.4	38.9	1.0	1.7	1.3	100.0
TENURE (years)									
0 to 2	15.5	11.5	21.1	17.0	28.5	.4	4.8	1.4	100.0
>2 to 5	15.7	9.4	19.2	19.6	30.4	0.4	4.4	1.1	100.0
>5 to 10	11.1	8.9	5.2	20.1	40.9	0.3	2.6	1.1	100.0
>10 to 20	10.3	9.0	12.8	23.5	40.9	0.5	2.0	1.2	100.0
>20 to 30	8.3	9.1	9.9	29.0	39.4	1.1	1.6	1.6	100.0
> 30	.3	13.3	7.8	35.7	32.1	2.3	1.0	1.6	100.0
All	9.5	9.8	11.4	26.4	38.9	1.0	1.7	1.3	100.0

Figure 5

Average Account Balance by Age and Tenure, 1998

(dollars)



Source: Tabulations from EBRI/ICI Participant-Directed Retirement Plan Data Collection Project

401(k) Investing *continued on next page*

401(k) Investing *continued from previous page*

CONCLUSION

Total 401(k) assets are more heavily invested in equities (defined broadly to include employer securities) than the universe of defined benefit plans. Nearly one fifth of participants have more than 80% of their account balance in equities; while one sixth have no money in equities. As a result, long term returns will vary substantially. Participants did not appear to have an asset allocation target that they rebalanced to during the 1996 to 1998 period.

This suggests that education continues to be a significant need, with the possibility of a need for active investment advice or direction for many participants in order to assure diversification and re-balancing.

Related to proposals for Social Security Individual Accounts, it underlines the need to do analysis based upon alternative asset allocations, not one averaged allocation, in order to reflect the likely range of outcomes if investment discretion is provided.

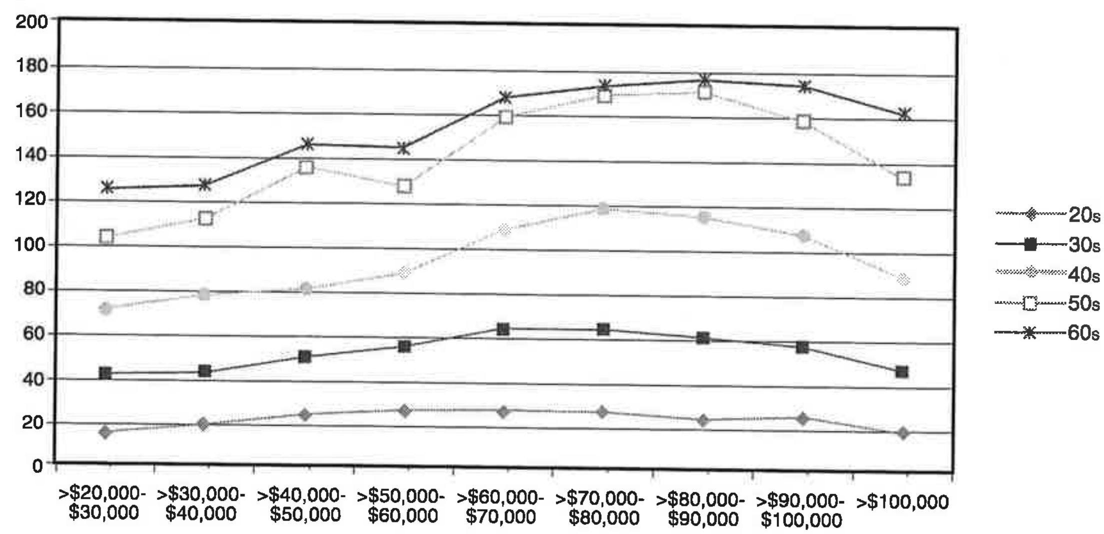
1999 data is now being entered into the EBRI/ICI database which will be released in the months ahead.

Excerpted from: "401(k) Plan Asset Allocation, Account Balances, and Loan Activity in 1998," EBRI Issue Brief no. 218, February 2000, Employee Benefit Research Institute,Washington, DC.

Dallas Salisbury *is the President and CEO of the Employee Benefit Research Institute or EBRI. EBRI, founded in 1978, is a Washington-based think tank dedicated to providing the latest objective and unbiased information on key employee benefit issues.*

Dallas is an authority on benefit trends and public policy issues. Dallas' article, 401(k) Investing - A Look At The Data, explores participant asset allocation based on the EBRI/Investment Company Institute Participant-Directed Retirement Plan Data Collection Project. The three-year effort looks at asset allocation during 1998 for 7.9 million active participants in 30,102 plans with $372 billion in assets.

Figure 6
Ratio of 1998 Account Balance to 1998 Salary for Participants by Age Group
(percent)

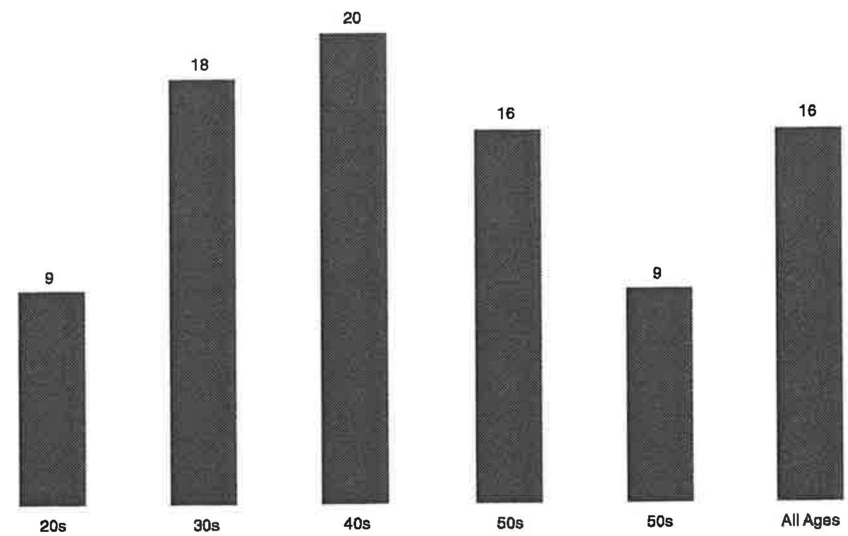


Source: Tabulations from EBRI/ICI Participant-Directed Retirement Plan Data Collection Project

401(k) Investing *continued on next page*

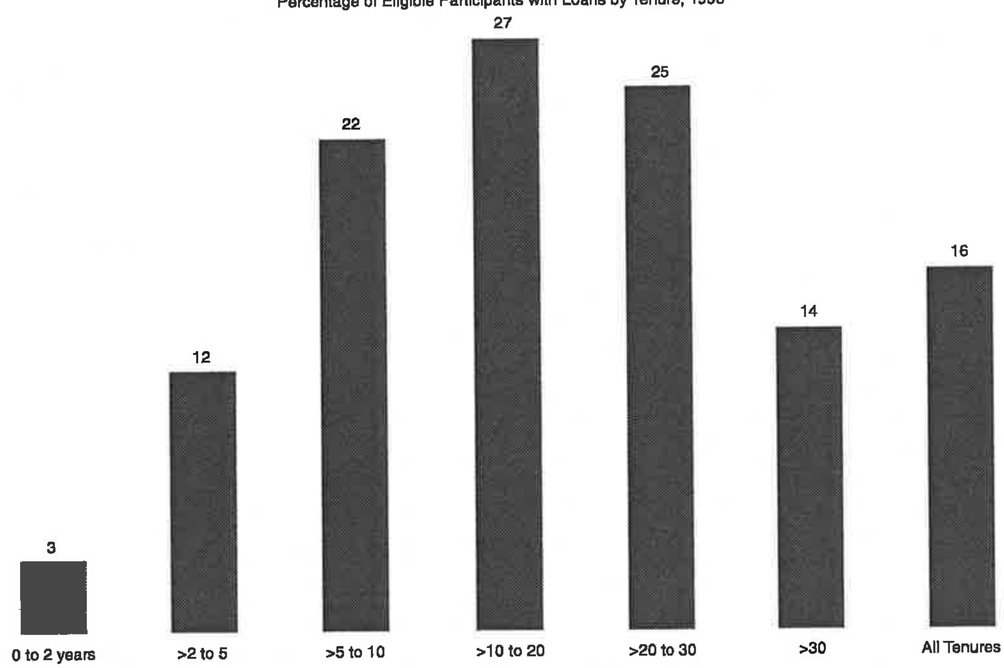
401(k) Investing *continued from previous page*

Figure 7
Percentage of Eligible Participants with Loans by Age, 1998



Source: Tabulations from EBRI/ICI Participant-Directed Retirement Plan Data Collection Project

Figure 8
Percentage of Eligible Participants with Loans by Tenure, 1998



Source: Tabulations from EBRI/ICI Participant-Directed Retirement Plan Data Collection Project

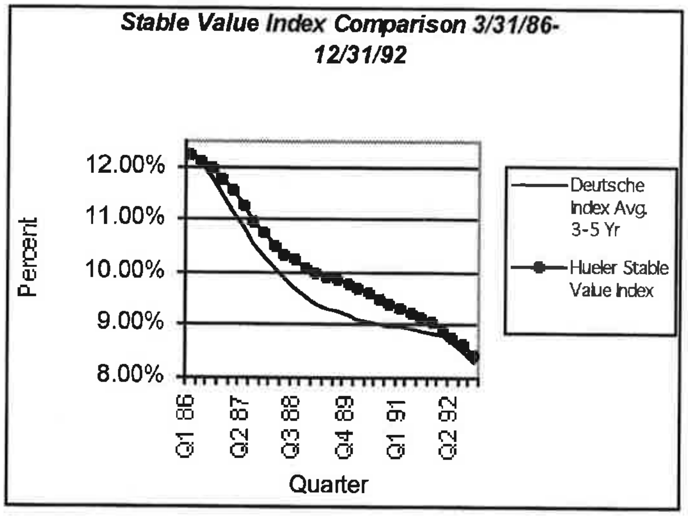
New Evaluation Tools Available to Stable Value Investors

By Janet Jasin Quarberg, Hueler Companies

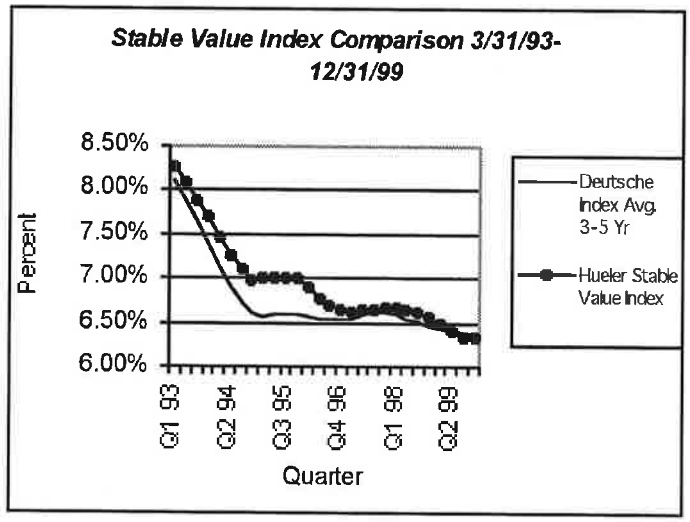
Stable value investors now have access to a new performance measurement and portfolio evaluation tools, with Hueler Companies' new "Separate Account" Stable Value Performance Index and Aggregate Industry Reports. Hueler has developed a comprehensive database of Stable Value information and has constructed an empirical return series that encompasses actual portfolio returns and investment strategies of close to 300 separately managed stable value funds.

Hueler's new Performance Index is different from other available indices, as it is not a theoretical portfolio constructed from illustrative GIC rates, but rather actual portfolio returns from several hundred Stable Value Funds. These funds employ a variety of sophisticated investment strategies and buy from a full spectrum of available stable value products. The Index is the (non-dollar weighted) average return of separately managed stable value funds provided from 16 investment managers and individual plan sponsors with stable value asset totaling approximately $75 billion. The index has an average credit of Aa1/AA, an average duration of 2.43 years, and the average Stable Value fund size is $257 million. All return numbers have been carefully compiled on a consistent basis and are gross of stable value manager fees and net of contract or product fees.

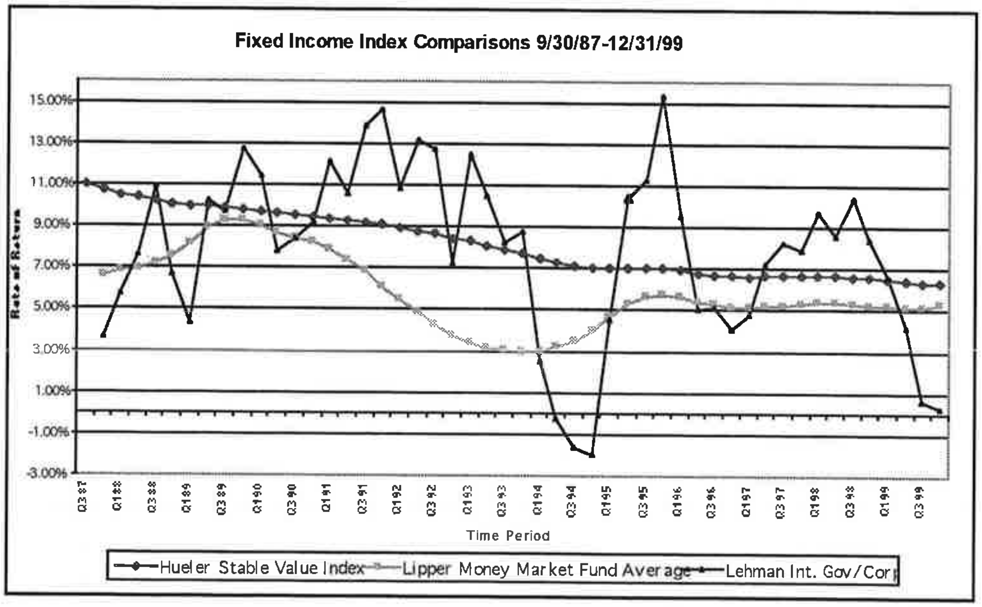
In the past, the average of the Deutsche (formerly the Bankers Trust Index) 3 year and 5 year Indices has commonly been used in the industry as an indicator of return. The return of Hueler Stable Value Index shows a consistent pattern of return as the Deutsche Index, but at slightly higher levels as shown in the charts below.



Stable Value Index Comparison 3/31/86-12/31/92



Stable Value Index Comparison 3/31/93-12/31/99



Fixed Income Index Comparisons 9/30/87-12/31/99

On a three, five and ten year annualized basis, the Deutsche index has yielded a 6.47%, 6.51% and a 7.27% respectively and the Hueler Index has yielded a 6.51%, 6.64% and a 7.47%.

The new Hueler Performance Index also shows very favorably when compared with the indices of other traditional fixed investment alternatives as shown in the chart below.

New Evaluation Tools *continued on page 17*

New Evaluation Tools *continued from previous page*

12/31/1999	Hueler Stable Value Index	Lipper Money Market Average*	Lehman Intermediate Gov/Corp
1 Year Return	6.33%	5.32%	0.29%
3 Year Return	6.51	5.28%	5.47%
5 Year Return	6.64%	5.35%	7.08%
5 Yr. Annual Standard Deviation	.24 %	.24 %	5.60 %

The Lipper MM returns have been grossed up by an average Lipper fee of 39 bpts.

On a three-year annualized basis as of 12/31/99, the Hueler Stable Value Index returned 6.51% while Money Markets returned 5.28% and Intermediate Bonds returned 5.47%. On a five-year basis, Stable Value and Money Markets had the same standard deviation, but Stable Value offered over 125 basis points more in return. Intermediate bonds on the other hand, provided just over 40 basis points of additional return over Stable Value, but with almost 25 times more volatility as noted in the standard deviations in the table found above. The Hueler Index data shows that Stable Value continues to provide very strong risk adjusted return relative to all its peers.

The following investment managers and individual plan sponsors are committed contributors to the Index and we hope to continue to bring on new participants each quarter.

American Express, Bell Atlantic, Certus Asset Advisors, Deutsche Asset Management, Dwight Asset Management, Dupont, Eli Lily, Fidelity Investments, Galliard Capital Management, Halliburton, IBM, Merrill Lynch, Putnam Investments, State Street Global Advisors, T. Rowe Price Stable Value Asset Management, and the Vanguard Group.

In the coming months, Hueler will be working with these managers to develop data subsets and criteria for relevant composites. Using manager input, Hueler will create standard composites that will be made available to the market on a regular basis and will also create custom composites upon request. In addition, Hueler will begin a new series of aggregate reports profiling purchase activity. These reports will highlight quarterly placement volume, contract type allocations and maturity selections. Hueler Companies currently produces a package of 25 aggregate reports covering the following key market statistics and plan characteristics: performance, maturity, quality, variability of return, cash flow, fund size, investment option allocation, asset class distribution, withdrawal methodology, transfer frequency and restriction provisions.

Whether you are looking to benchmark a portfolio or communicate to management, participants, or outside professionals, the new Stable Value Performance Index and Aggregate Market Reports can be used to significantly improve the process. This new data also provides managers, plan sponsors, consultants and issuers with the tools necessary to more effectively communicate the positive attributes of stable value investments relative to other fixed income options and to better articulate the role stable value should play in the asset allocation decision process.

Lipper Rates Stable Value Fund #1 in Fixed Income

BT Pyramid Mutual Funds: Deutsche PreservationPlus Fund; Institutional Class was rated number one within the Intermediate Investment Grade Debt Fund category by the Lipper Fixed Income Fund Performance Analysis Service for 1999. Deutsche Asset Management was also the first to present the features of stable value: principal preservation with the returns of intermediate term bonds minus the volatility in a mutual fund platform in October 1997.

What AICPA SOP 94-4 Hath Wrought: The Demand Characteristics, Accounting Foundation and Management of Stable Value Funds

By Paul J. Donahue PRIMICO Capital Management

SUMMARY

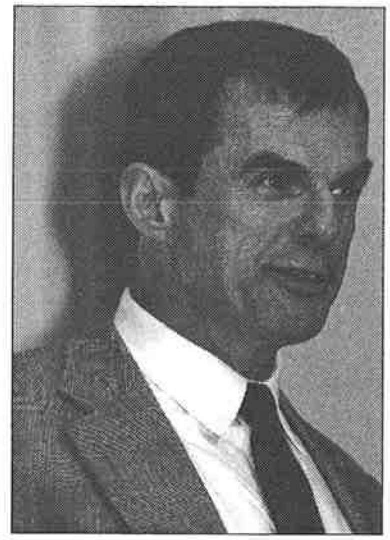
AICPA SOP 94-4 is the foundation of the Stable Value Option ("SVO"). A SVO guarantees the principal and accrued interest of participant benefit payments and transfers. The Article analyzes market demand and identifies legitimate participant expectations. It concludes that guarantee of principal is the bedrock of the SVO's appeal to the conservative investor. Level of return, though important, is secondary. The Article establishes the absolute superiority of SVOs over money market funds as retirement income vehicles.

On the basis of this economic analysis, the Article develops the implications for SVO portfolio management policy and practice.

The Article discusses in detail AICPA SOP 94-4. It concludes that the basic requirements do full justice to legitimate participant expectations, but that exceptions permitted by example unduly erode the guarantee.

The Article moves on to discuss contract provisions required, in view of marketplace assignment of risks, to assure that SVOs meet participant expectations. It concludes that assignment of default risk to participants is economically efficient since otherwise credit analysis would be wastefully duplicated. It notes that failure to constrain permissible issuer termination rights is the greatest weakness of SOP 94-4, since an issuer right to terminate at will makes a guarantee worthless. The article sets out the conditions that should exist to justify termination for cause and applies them to "termination for cause" clauses frequently seen in practice. The Article finds limits on the guarantee for "employer-initiated" events economically unsound, but those for "plan events" economically justified. The Article favors arbitration provisions, and comments briefly on other contract clauses.

The Article discusses the evolution of SVO management from insurance company blended rate products, to plan-specific new money rate contracts, to Guaranteed Investment Contracts, to insurance company separate accounts, to guarantee contracts "wrapping" portfolios of readily marketable assets.



The Article goes on to discuss the formulation and implementation of investment strategy for SVOs in today's environment. It emphasizes the importance of credit analysis in view of the need to preserve principal, and the importance of investment objectives and guidelines that reflect the realities of the SVO's market demand.

The author wishes to express his thanks to his PRIMCO colleagues, especially to Dennis T. Donahue, James F. Guenther, W. Bruce Harley, Kevin Horsley, Stephen M. Johnson and Stephen F. LeLaurin, for their invaluable assistance in writing this Article.

Paul Donahue *is Director of Product Development for PRIMCO Capital Management, a manager of Stable Value Option funds. He is a graduate of Dartmouth College, and has his Ph.D. and J.D. degrees from Yale University. He is a Fellow of the Society of Actuaries and a member of the American Academy of Actuaries. He is a CFA candidate, and passed the Level 11 exam in June, 1999.*

Global Opportunities for Stable Value

SVIA is pleased to announce that "The Global Opportunities for Stable Value Report" will be available in early April. This report brings together a wide range of information on opportunities to introduce and expand stable value products worldwide. This compilation also provides an overview of the distinct and different markets for qualified retirement plans and other non-qualified principal protected products.

Many thanks go to the members of the Working Group on Global Opportunities for pulling together this information. They are:

Wendy Cupps, PIMCO
Chip Gillis, Bear Stearns
Tom Hartlage, AEGON Institutional Products
Greg McGreevey, ING Institutional Markets
Tom Obsitnik, Eli Lily and Company
Perry Shwachman, Katten, Muchin & Zavis
Ken Walker, T.Rowe Price
Robert Whiteford, Bank of America
Mike Wyatt, Dupont Capital Management
Larry Zimpleman, The Principal Financial Group

Ken Walker deserves special recognition for leading this effort. Our thanks also go out to John Milberg, Wendy Cupps, Bob Whiteford; and Deutsche Asset Management's Eric Kirsch, NatWest's Christina Aragon and PRIMCO's Paul Donahue who were recruited for this effort. These individuals went beyond the call of duty, lending their expertise to the research, review and editing of this report.

CONGRESS HOLDS HEARINGS ON ERISA REFORM

By Donald J. Myers, Reed Smith Shaw & McClay, LLP*

Congress is concerned that certain provisions of ERISA may have become outdated in the 25 years since ERISA was enacted. To address this concern, the House Education and the Workforce Subcommittee on Employer-Employee Relations has undertaken a series of hearings to discuss current ERISA issues, and to figure out what changes may be necessary to modernize the statute.

According to Rep. John Boehner (R-Ohio), the Subcommittee chairman, some of the principal issues are in the investment area. The economy has changed considerably since 1974, as has the nature of retirement savings. In his opening remarks at the first hearing, he stated that "To the extent we can make pension and retirement investment more efficient — allowing participants to maximize returns on their investments and allowing them access to better information about their investment options — we will have served our constituents well." In an effort to make the hearings bi-partisan, he is working closely with Rep. Robert Andrews (D-N.J.), the ranking Democratic member.

At the first hearing, held on February 15th, the subcommittee members heard from four authorities on ERISA, drawn mainly from academia. At the second set of hearings, held on March 9th through 10th, they heard from witnesses representing industry and industry associations, as well as labor and pension rights groups. At the next hearing, which has not yet been scheduled, the subcommittee intends to hear from the regulators, principally the Department of Labor.

In line with Rep. Boehner's emphasis on investment issues, the principal topics addressed at the hearings were investment advice for plan participants and the ERISA prohibited transaction rules. Several other issues also were raised by the witnesses as possible areas for ERISA reform.

INVESTMENT ADVICE

Acknowledging the general shift in the pension area in favor of participant-directed defined contribution plans, the witnesses emphasized the importance of participant access to investment education and advice. Several, such as Prof. John Langbein of Yale and Allen Reed of the Committee on the Investment of Employee Benefit Assets (CIEBA), pointed out the considerable growth of defined contribution plans in the past 25 years, placing investment risk on employees. As a result, they said that there is a need for the employees to be able to obtain professional, individualized advice to help them manage their accounts.

The problem is in providing access to such advice. The witnesses pointed out that current law, by subjecting investment advisors to fiduciary standards and the ERISA prohibited transaction rules, discourages employers and investment firms from making advice available to plan participants. Prof. Langbein advised revisiting those barriers under ERISA that prevent employers and investment intermediaries from giving individualized advice to plan participants. Kenneth Cohen of Massachusetts Mutual Life Insurance Company was more specific, suggesting that Congress provide a statutory exemption from the ERISA prohibited transaction rules for investment education and advice. Witnesses from the Securities Industry Association and the Frank Russell Company suggested that such an exemption could rely on disclosure standards to protect plan participants.

Not all the witnesses came out as strongly in favor of creating special rules for investment advice. The AFL-CIO was concerned about potential conflicts of interest that could arise from fund providers providing advice. One of the strongest cautions about potential conflicts came from Joseph Grundfest of Financial Engines, an independent advice provider, citing the potential dangers of permitting fund providers to advise participants in a manner that could promote the funds' interest in obtaining higher fees. However, in response to questions, he acknowledged that the shady practices such as he was suggesting were not widespread in the mutual fund industry, and other witnesses challenged his assertion that fund providers were affected by "secret biases" in providing investment education and advice programs.

PROHIBITED TRANSACTION RULES

After investment advice, the second major focus of the hearings was on the ERISA prohibited transaction rules.

Prof. Langbein and John Shoven of Stanford University called for the complete abolition of the ERISA prohibited transaction rules, with Prof. Langbein observing that "the prohibited transaction rules do badly what ERISA's core fiduciary law does well." Prof. Langbein's objection was that the rules are redundant with the duties of loyalty and prudence and overbroad, requiring a vast body of "excusing law" to prevent innocuous conduct from violating the prohibitions. Any conduct appropriately forbidden by these rules, he said, is already forbidden by the core fiduciary rules of section 404(a), so that the rules serve only to prevent plans from engaging in beneficial investment transactions and increase the marginal cost of most non-public transactions.

On top of that, the regime "needlessly aggrandizes the power of the regulators," he added.

At the other extreme, several witnesses came out against any changes to the ERISA prohibited transaction rules. Prof. Teresa Ghilarducci of the University of Notre Dame and benefits attorney Michael Gordon emphasized the possible abuses that could result from weakening the current rules, as did the AFL-CIO testimony. They concluded that the rules should be retained to preserve their deterrent effect.

The industry witnesses generally came out in between the two

ERISA Reform *continued on page 20*

ERISA Reform *continued from page 19*

extremes. While not calling for repeal, they described the problems created by the broad scope of the prohibited transaction rules and the difficulty in obtaining exemptive relief. Rep. Andrews agreed, citing the statistic that half of the exemptions requested take over 18 months to be resolved. Kenneth Cohen of Massachusetts Mutual recommended narrowing the statutory definition of "party in interest" to exclude unaffiliated service providers, and permitting transactions that meet arm's-length terms and disclosure standards. Most of the others focused their recommendations in this area on the more limited issue of investment advice.

A specific issue raised in connection with the prohibited transaction rules was the cross-trading of securities, a matter currently under consideration by the Department of Labor's Office of Exemption Determinations. Prof. Ghilarducci and Mr. Gordon did not think that Congress should take any action on cross-trades. Prof. Ghilarducci argued that permitting cross-trading would increase rather than decrease plan costs, while Mr. Gordon said that the exemption process should be allowed to play out on this issue. Others, such as CIEBA, argued that the exemption process should give more weight to the benefits that cross-trading has to offer.

EMPLOYER STOCK INVESTMENTS

Another subject raised by some of the witnesses was the ability of plans to invest in employer securities. Prof. Langbein argued that the diversification and self-dealing rules of ERISA should apply to 401(k) plan investments in employer stock, because employer stock investments present serious risks to plan participants. Prof. Ghilarducci argued for limiting the permitted amount of company stock in individual participant accounts.

OTHER ISSUES

Several witnesses emphasized problems with pension coverage, including Prof. Ghilarducci, Mr. Gordon, and representatives of the Pension Rights Center and the Older Women's League. They called for several reforms to improve coverage, such as extending coverage to part-time and temporary workers and accelerating vesting requirements.

Mr. Shoven called for several simplification measures. These included replacing the Internal Revenue Code nondiscrimination rules and repealing the minimum distribution rules.

CURRENT STATUS OF ERISA REFORM

At the end of the March 10th hearings, Rep. Andrews summarized the testimony thus far. He said that there had been general agreement that the basic precepts of ERISA - voluntary employer cooperation and strong fiduciary standards - are working. The witnesses had generally agreed that there should be more flexibility to enable employers and service providers to give individually tailored investment advice, while protecting against biased advice and conflicts of interest. While no one had advocated changes that would allow self-dealing, there was concern about the prohibited transaction rules burdening plans with needless transaction costs. However, there was no consensus on any legislative steps that need to be taken to address these issues.

At the next hearing, the subcommittee members should have the opportunity to ask the regulators about the issues that have been raised to date and to explore possible solutions. Whether the process will in fact lead to ERISA reforms, and the nature of those reforms, remains to be seen.

**Michael B. Richman of Reed Smith Shaw & McClay assisted in the preparation of this article.*

Dateline Wall Street... "Relax. Stocks Rarely Steer the Economy," *New York Times 9/3/98...*"Dow Finishes Day Over 10,000 Mark for the First Time," *New York Times 3/30/99...*"Investor Fears of Rising Rates Sends Stock Market Plunging," *New York Times 2/25/00...* "Dow Falls for the Day But Has Record Week," *Washington Post 3/18/00...*"If You Think Last Week Was Wild..." *New York Times 3/19/00...*

Count on one thing: SVIA's 2000 National Forum
October 10 – 12 at the Monarch Hotel in Washington, DC.