

Department of Labor/Department of the Treasury
Joint Hearing on Lifetime Income Options
September 14, 2010

Welcome

Robert Doyle:
Good morning everyone.

Male Speaker:
And how are you?

Male Speaker:
Nice to see you.

Robert Doyle:
I'd like to welcome you all to the Department of Labor and the joint Department of Labor/Department of the Treasury Hearing on Lifetime Income Options. We're going to start this morning with some brief opening remarks from Assistant Secretary Phyllis Borzi and J. Mark Iwry, special advisor to the secretary of the Treasury and deputy assistant secretary for health and retirement policy at the Department of the Treasury. With that, Ms. Borzi?

Phyllis Borzi:
Thank you, Bob. Good morning everyone and welcome to the Department of Labor. As Bob said, my name is Phyllis Borzi, and I'm the assistant secretary for the Employee Benefits Security Administration. I'm really excited to be here today, and I'm really happy that all of you can join us. We're really excited that so many people have expressed interested in this very, very important topic of lifetime income streams. And we especially welcome our partners from the Treasury and the IRS in this discussion and in the project as a whole.

As you know, the retirement system has changed dramatically over the last several decades as the emphasis has shifted from defined benefit to defined contribution plans. And with that shift, workers are bearing a much greater level of responsibility for the management of their retirement savings. Many workers now spend their entire career trying to save enough so that when they retire they can maintain a comfortable standard of living. But when they do retire, one of the biggest questions they face is, in what form should they take their retirement benefits? Should they

receive it in a lump sum, in a stream of income or some other form? For most, especially workers in 401k plans, this really means getting all of their money at once in a lump sum, and one of the reasons for this outcome is that most 401k plans do not offer any other option. They don't offer a lifetime income stream. And in fact, in 2009, only 15 percent of defined contribution plans -- participants had the option of receiving their benefits in a lifetime stream of income. But we know from the statistics as well, that unfortunately, when people are offered annuities or other forms of lifetime income streams they often don't take it. They prefer to receive their assets in the form of a lump sum distribution.

And that's fine. That's fine for some people because lifetime income is not for everybody, but in doing so, in deciding to take their benefits in a lifetime income stream, some issues are presented for workers because it means they have to manage their money in a way that ensures that they don't outlast their retirement assets, and it also means bearing the risk that investment turns -- investment returns may turn negative and actually deplete the value of some of those assets. So, it's this very real challenge that was the primary reason we decided to launch this national dialogue around lifetime income options. We wanted to learn what options were available in the marketplace to participants now and how to use your experience, the private sector's experiences and expertise, to help our two departments determine what steps if any we can take to increase the options available to individuals as they grapple with these important financial decisions.

First step in this process, as you know, was the RFI, the request for information. It engendered hundreds of comments and some very strong opinions on all different sides of the issue. And I want to thank everybody in the room here who submitted comments and those who may be watching this webcast for the comments they provided us. The hearing -- this hearing is a second step in this dialogue and is going to help -- we hope -- to clarify some of the technical issues and insights that were provided in those submissions. I'm excited about this hearing and confident that we'll learn more about this issue.

The next two days are going to be full, I hope, of rich and very informative testimony and equally interesting dialogue. The issues we're talking about today and

tomorrow are very difficult and complex ones and as I've said, probably many of you have heard me say many times before, we don't come to this with any preconceived notions about what the outcome should be. We don't know what the next steps will be. As a matter of fact, it's entirely possible that we might conclude that there are no next steps for the government to take. But this is a dialogue we think is very important to have and as I said before the entire effort here is designed to focus on whether there are ways that we can offer retirees other options.

And so I appreciate your willingness to come and help us out, think through these issues -- work through these issues and help us figure out what steps might be necessary and helpful to our American workers. So, thanks again for coming and I look forward to hearing your testimony. I will be, unfortunately, in and out but I hope to be here for most of the day today. So, thanks again and thank you to our panel.

J. Mark Iwry:

Phyllis, thank you and to all of our colleagues at the Department of Labor, all of you who are here and those who are listening to or watching this remotely who've been participating in this national dialogue. We appreciate your input. The written comments have been exceedingly useful and thoughtful.

As most of you know, this dialogue hearing today, the related requests for comments previously, is in the context of the department's support for the private pension system and especially for employer sponsored retirement plans, both defined benefit and defined contribution. We see this as a dialogue that is about choices -- about enhancing the choices, the options, that participants have for managing their retirement savings and to solicit comments and input on whether and, if so, how the departments might give participants better opinions for managing their savings and for accessing lifetime income or other arrangements designed to provide a stream of income after retirement.

As described in the RFI, individuals have been increasingly receiving their savings in the form of an account balance that they manage during their retirement years rather than as a pension for life of the type traditionally provided by a defined benefit pension plans and in that context, we want to see whether there is anything we can do that's

constructive to be of assistance in helping participants have better choices, better options, relative to receiving their income as a stream or managing their assets after retirement.

The RFI and this dialogue does not reflect any intention to require a purchase of annuities or any other particular investment nor are the questions in the RFI or in the document that preceded this hearing designed or intended to provide a basis for requiring any such purchases. We're here to consider whether and how we might increase people's choices, not limit them. We're in a listening mode, and we're ready to start listening. So we look forward to your statements and discussion. Bob?

Robert Doyle:

Thank you, Mark. As most of you are aware, we did -- the agencies did jointly publish a request for information. We received almost 800 responses to that request. Suffice it to say, it was a kind of a very, I think, exciting beginning to, as I think both Mark and Phyllis referred to as a national dialogue on an important issue of expanding options, for participants in the private sector, pension plans. I'm very happy that we were able to accommodate all the timely requests that we received to participate in this hearing which we'll be conducting over the next two days. Unfortunately, given the number of requests that we have and competing schedules of the panelists, we're going to have to limit the dialogue during this particular hearing to those who are testifying today. But we are keeping the public record open for 30 days and invite anyone who has not had an opportunity to participate today or tomorrow to submit written comments to the agencies, and those comments will be available and include as part of the record and posted on our website, and I believe they'll also be posted on regs.gov as part of our normal comment process.

A few administrative matters, we will follow the agenda that was published and if you don't have that I think we had a few copies at the entry. We will be calling the panels in order and probably referring to them by number. If you have any questions as to what panel you're on or what number that panel is and you don't have an agenda, please see Janet Walters. Janet, please raise your hand.

We will make every effort to stay on schedule during the hearing and in that regard, have two requests for those

testifying. First, if you could identify yourself, in terms of your affiliation, who you're with, as well as the organization you're representing that would make our job and the job of the transcribers easier. Second, and most importantly, we're going to ask that you stay within you're allotted time, generally ten minutes. We do have a timer that will help you in that regard --

[laughter]

-- it will count down and share with you the amount of time you have left and at the expiration of that period there will be a very subtle chime that will notify everyone of the expiration of your allotted time frame.

The government panel will defer questions to the end -- the completion of each testifying party on each panel with regard to those questions, we are interested in exploring a wide variety of issues from a variety of perspectives. Therefore, we strongly suggest you not infer any particular views or policies or positions from any of the questions that the panelists, at least on our side, ask. I should also note there will be periodic changes on the government side into arms of the participating panels to accommodate various schedules, and we'll try to keep you apprised of those as those take place.

Finally, I should note, the proceeding is being webcast live and will be available on the EBSA website in archive form.

So with that, I think I will now introduce my fellow panel members. To my immediate right, Michael L. Davis, deputy assistant secretary for the Employee Benefits Security Administration; to his right, Alan D. Lebowitz, deputy assistant secretary for program operations, also EBSA; Joe Piacentini; to his right is director to our office of policy and research, Mr. Iwry; and Patricia McDermott who's with the Office of Chief Counsel, IRS. With that completed, we'll now invite our first panel to join us.

I don't know whether you've agreed on a particular order, but if not, why don't we follow the order of the agenda, and we'll start with Ms. Boyd.

Panel One

Janet Boyd:

Thank you. My name is Janet Boyd, and I am the director of Government relations tax and benefits for the Dow Chemical Company. I am testifying today on behalf of the American Benefits Council. My testimony focuses on the fiduciary barriers and the disclosure and education needs of lifetime income products from the perspective an employer.

The Council is a public policy organization representing principally Fortune 500 companies and other organizations that assist employers of all sizes in providing benefits to employees. Collectively, the Council's members either sponsor directly or provide services to retirement or health plans that cover more than one hundred million Americans. I serve on the Council's board of directors and actively participate both directly and through the Council in public policy discussions regarding benefits issues confronting my company which is typical of companies providing retirement benefits to employees.

At the end of 2009, Dow employed approximately 52,000 people worldwide. About 24,000 of Dow's employees are in the U.S. and Dow supplies retirement benefits to more than 100,000 retirees into the U.S. Specifically, Dow supplies a range of retirement benefits for its U.S. employees, including a defined benefit plan, a 401k plan, and health benefits. U.S. employees are eligible to participate in defined contribution plans by contributing a portion of their compensation, which is partially matched by the company.

New Dow employees are automatically enrolled with an opt out option in the 401k plan, within 60 days following their date of hire and three percent of base annual compensation is contributed to the plan as a pre-tax contribution, with company matches as well. If the employee fails to designate an investment option, their contributions will default to an applicable life cycle fund based on the date of birth. Additionally, under the automatic enrollment program, employee contributions are automatically increased each year effective April 1 by one percent until the employee reaches a contribution rate of six percent. Employees can also voluntarily participate in the automatic increase program. Dow's plans also allows

employees the option to make [unintelligible] 401k contributions and post-tax contributions.

Dow allows our 401k participants to receive distributions in lump sum which can be rolled over to an [unintelligible] or other non-Dow pension plan or they can roll over their accounts to the Dow defined benefit pension plan, subject to specified maximum and minimum amounts. Such roll-over will be converted to an annuity and paid according to the terms of the Dow defined benefit plan. We do not offer any other lifetime income options at this time.

Dow's 401k plan has approximately 40,000 participants and more than \$6.1 billion in assets. Approximately 88 percent of our active employee population is enrolled in and contributing to the plan.

Our employees also have access to our defined benefit plan as I mentioned with most of our employees hired before 2008 under a pension equity plan design and the remainder under a more traditional cash-balance plan design, qualified and designed under the Pension Protection Act. In 2009, Dow contributed \$355 million to its pension plans, and we expect to contribute about \$304 million in 2010. Our contributions reflect the strong support received from our employees for our retirement program, which as previously mentioned, also serves as an access to lifetime income products. Accordingly, we urge both the Department of Labor and the department of Treasury to issue guidance as soon as possible under PPA that facilitates account-based plans, particularly pension equity designed plans.

Dow continues to evaluate the potential for offering more lifetime income options within its 401k plan. However, our assessment today is that the current market is too immature to move in that direction any time soon, and we welcome the development of public policies that would facilitate the design of new options that are less complex and have lower costs than available today.

The notice of this hearing requests testimony on the fiduciary safe harbor for a selection of lifetime income issuers or products and for planned sponsors desiring to add lifetime income products to their plans. As I mentioned previously, Dow has not incorporated any lifetime income products to our plans other than the option to roll over into our qualified defined benefit plan. The most

significant obstacles to Dow and other Council companies are fiduciary concerns. Under current law, the selection of an annuity provider is fraught with potential missteps that could result in continuing liability for the plan sponsor well into the future. To rectify this, plan sponsors need clear, simple, fiduciary guidance allowing them to make lifetime income options available to plan participants without risking a significant increase in potential liability.

Although Department of Labor guidance does make clear that the safest available standard in Interpretative Bulletin 95-1 does not apply to the selection of annuity contract provider for distribution from a defined contribution plan, the guidance requires significant due diligence on the part of plan sponsors without a clear safe harbor in our and the Council's view. This due diligent includes an assessment of the annuities providers continuing ability to fulfill its contractual obligations and plan sponsors including Dow are understandably concerned that courts will make that assessment with the advantage of hindsight resulting in potential litigation liability years later. A clear, simple safe harbor is a necessary first step to increase the interest of plan sponsors in adding lifetime income options to their plans.

Many Council companies are starting to focus on lifetime income products that allow plan participants to roll over their plan benefits into an IRA with an annuity platform which allows the IRA to obtain multiple bids from different insurance companies selling annuity products. This isn't too different from plan sponsors like Dow do now, which allow rollovers to qualified pension plans. However, we would urge DOL to provide a safe harbor that would address fiduciary liability concerns that plan sponsors currently have if they inform participants about the availability of the annuity platform for rollover IRAs without any endorsement that could imply fiduciary responsibility. Specifically, we need clear guidance from the department indicating the necessary due diligence steps that could be taken by plan sponsors to avoid future liability. If plan sponsors are encouraged to provide access to such annuity platforms for rollover hours without becoming subject to fiduciary liability, more plan participants would have access to lifetime income products.

The Council's companies also strongly believe disclosure and education are the first steps toward increasing the availability and appropriate use of lifetime income products. The Agency should encourage but not require defined contribution plan sponsors to provide illustrations of how account balances translate into lifetime payments at age 65 by publishing model disclosures which if used, would not give rise to fiduciary liability. The Department of Labor could provide examples in the model. For example, a lump sum of "X" could create an income stream of "Y" at age 65 providing the relative interest rate and mortality assumptions. The model could also show the variants based on different interest rates to avoid employee relations problems whenever interest rates decline and future illustrations show lower payments.

Though Council is also a strong proponent of financial literacy education and agrees with the agencies that educating participants on the management and spend-down [spelled phonetically] of retirement assets is a crucial goal as an increasing number of baby boomers reach retirement. However, plan sponsors who want to educate their employees on the benefits of lifetime income and other management and spend-down concepts may be deterred by the lack of guidance on how to provide appropriate education in this area without triggering fiduciary liability.

The Department of Labor's Interpretative Bulletin 96-1 which provides detailed guidance on the difference between investment advice and investment education has been very useful for both plan sponsors and participants, resulting in increased investment education that otherwise likely would not have been provided. Expansion of this interpretive bulletin to cover education on the management and spend-down of retirement benefits could have a similar effect on educating participants on the concepts they will need to know for the retirement phase. Similarly, the Council recommends expansion of the Department of Labor's advisory opinion, commonly known as SunAmerica, to address computer advice on the spend-down of retirement benefits.

Again, thank you for providing me this opportunity to present the Council's testimony from the perspective of a plan sponsor. I welcome any questions you may have.

[chime noise]

[laughter]

J. Mark Iwry:

Bob? I assume there'll be a chime for the government panelists as well [unintelligible]?

Robert Doyle:

We are off to an auspicious start, I must say.

[laughter]

Mr. Wray?

David Wray:

Good morning. I am David Wray, president of the Profit Sharing/401k Council of America, an association of employers that provides profit sharing and 401k plans for their participants.

The looming retirement of the baby boom generation has resulted in an increased focus on the 401k retirement distribution phase by those in the employer-provided retirement plan community. At the same time, retirement plan participants continue to take their retirement distributions in lump sum form. Less than one percent of defined contribution plan participants selected annuity distribution option when one is offered. Defined benefit pension plans are experiencing a similar lack of participant interest. For the one half of defined benefit plans that offer a lump sum payment, more than 90 percent of participants endure the cumbersome spousal waiver procedures to avoid the otherwise required annuity distribution.

A major factor in the limited usage of annuities in retirement plans is that the average wage worker already is provided with a substantial annuity when he retires or she retires. According to the 2010 Social Security Trustees Report the average 65 year old retiring in 2010 will receive an inflation index Social Security benefit that replaces 40.8 percent of preretirement income. If the average retiree seeks to replace 80 percent of their working income in retirement, Social Security will provide half of that amount -- index for inflation. In general, because participant interest is so low, defined contribution plan sponsors increasingly see no reason to

accept the additional fiduciary exposure that comes with an in-plan annuity option. As a result, the availability of annuity options in employer-sponsored defined contribution plans has been declining. In the Profit Sharing/401k Council of America's survey of 2009 plan [unintelligible] experience, 19 percent of plans offered an annuity distribution option. This is down from 23 percent in 2005 and 34 percent in 2000.

Notwithstanding the above, plan sponsors are becoming more interested in assisting their participants with transition from accumulation to retirement. PSCA recently surveyed its plan sponsor members and found that 91 percent of respondents are aware of retirement income products and only 17 percent felt the employer had no role in assisting their participants with retirement transition. Fifty-seven percent of plans now offer an installment payment option as well.

You have asked about participant concerns affecting the choice of lifetime income relative to other options. I would summarize these concerns in three general areas: fees, flexibility, and confidence. PSCA believes the market should be permitted to address fees and flexibility. The government has an important role in restoring and maintaining confidence in the financial services that support the annuity process. Historically, fees embedded in annuity products, especially retail annuity products have been sufficiently high enough to offset an annuities benefit of long-term security. Further, annuity solutions have been designed and marketed in a way that makes apples-to-apples comparisons difficult. Participants need access to institutionally group priced options presented in a way that permits them to maximize their purchasing power. Individual retirement situations vary widely, and participants need the flexibility to tailor solutions to fit their individual needs. They need access to a board range of annuitized options, the ability to annuitize only a portion of their assets, access to multiple providers so they diversify the investment risk, the ability to make multiple annuity purchases over time, and access to annuities with inflation protection.

The provider community is well aware of this situation and has responded by developing and marketing many new lifetime income products. Some are in-plan products that permit

investment during the accumulation phase. Others are distribution stage products with much more flexibility than the traditional products. A significant portion of the industry is marketing their annuities on an IRA platform like that provided by the Hueler Company's [spelled phonetically] income solution platform, rather than as a direct plan distribution option. The marketing is delivering solutions to these concerns about fees and flexibilities.

At the same time, confidence in our financial institutions has recently been dealt a significant blow. Annuities by their nature depend on the abilities of institutions to exchange dollars today to payments over decades. Unless plan sponsors and participants are confident that those selling an annuity today will be able to deliver the promised benefits tomorrow, they will be reluctant to annuitize plan assets. It is critical that the government take whatever steps are necessary to rebuild and then maintain the confidence of working Americans in our financial institutions.

You have asked about information to help participants make choices regarding management and spend-down of retirement benefits. While virtually all sponsors provide some type of education to plan participants, practices vary widely. In PSCA's 53rd annual survey, reflecting 2009 plan experience, 33 percent of responding sponsors provide education specifically relating to retirement distributions. In some cases, plan sponsors offer extensive pre-retirement education that addresses not only the employer's plan, but Social Security and Medicare and even estate planning. Other sponsors feel that education should be limited to the plan and its investment options.

PSCA believes that the current guidance regarding the provision of education or advise about distribution-related issues including the ability to use plan assets to educate participants about lifetime income or other arrangements is sufficient. However, if some need the Department of Labor to expand and clarify Interpretive Bulletin 96-1, so they can rely upon the bulletin in order to provide participants with information to help them make better informed retirement income decisions than the Department of Labor should do so.

Also, retirement decisions regarding plan assets are not made in a vacuum. Guidance clarifying that it is appropriate to use plan assets to provide for broad pre-retirement education that goes beyond the issues related to the plan or investing plan assets such as Social Security, Medicare, general estate planning, elder care, long term care, et cetera, will encourage more plan sponsors to provide this type of information and education to plan participants.

You have asked about the disclosure of account balances as monthly income streams. PSCA does not support a regulatory or congressional effort to require individual benefit statements to present an account balance as a stream of future lifetime income payments. That said, some plan sponsors and service providers voluntarily offer this feature today. Once again, PSCA believes that plan design decisions such as this are best handled by individual plan sponsors. Section 105 of [unintelligible] requires that benefit statements provided to participants and beneficiaries in self-directed, individual account plans include a notice directing the participant or beneficiary to an Internet website at the Department of Labor. The website includes a rich array of resources for participants. The department should consider adding an income stream calculator to the site that participants could use if they want to make this calculation. If the department agrees to this suggestion, the calculator could accommodate both insured products and noninsured structured payment products. S-3760, the Automatic IRA Act of 2010, sponsored by Senator Bingaman, includes a provision that closely tracks our recommendation.

You have asked about a fiduciary safe harbor selection of a lifetime income issuer or product. Fiduciary concerns are a major issue for plan sponsors that are interested in offering a lifetime income product. The current safe harbor guidance, while helpful, is not a safe harbor in the conventional sense. It merely lays out a subjective process that constitutes a prudent selection process for selecting an annuity provider. To effect a behavior change by plan sponsors the government will have to take responsibility for the safe harbor status of certain decisions, particularly the long term viability of a product provider.

You have asked about alternative designs of in-plan and distribution lifetime income options. We are pleased at the evolution and the philosophy regarding annuitization of plan assets. Rather than assume that full and immediate annuitization of plan assets at retirement is the best practice, it is now recognized that annuitization is a tool participants can use as they develop a custom-designed best solution. This has opened the door to a wide range of innovative products and approaches. Some products have an insured or annuity feature and others managed pay-out funds. Longevity insurance that begins payment at an advanced age provides an interesting complement to the managed pay-out funds and other insured products.

At the same time, it is currently difficult to include an in-plan lifetime income product with other investment options in a defined contribution plan that allows transfers between investment choices, because of surrender charges and fees. It is also difficult to help participants understand how accumulation annuities work in relation to other investment options and hard to find an investment model that would meet the needs of the general population of participants. Compliance with a joint and survivor annuity regime and required minimum distribution rules also adds some difficulty for these products. Portability issues arise when the participant severs employment. These products are now in their infancy and questions about them so far have resulted in a low adoption rate by plan sponsors. However, PSCA believes the market should be permitted to refine and improve these products without government interference that would enhamper [spelled phonetically] this important process.

When products are developed that meet the needs of participants and plan sponsors, they will be included in employer provided plans. This marketplace of ideas combined with the flexibility of the defined contribution system has resulted in continually improving retirement plans and we are confident that it will soon bring attractive lifetime income products to America's workers.

Thank you for the opportunity to share our comments with you and I look forward to the question and answer period.

Allison Klausner:

Good morning. My name is Allison Klausner, and I am legal counsel at Honeywell International. I support the legal compliance for the defined contribution plans.

I am here today on behalf of the ERISA Industry Committee, generally known as ERIC. As you know, ERIC is a nonprofit associate whose members are America's largest employers who directly sponsor comprehensive retirement benefits. I'm honored to serve as the chair of the ERIC's Taskforce on Lifetime Income.

Ms. Borzi summarized very well the issues of the landscape today of defined contribution plans for distributions. She described very well the challenges that our employees and our retirees face as they'd decide how to take their income from the retirement plans. I am aware that you have my written testimony and as such I am going to jump to the heart of my testimony today.

In recent years a tremendous focus has been on the accumulation of retirement fund assets and the desire to ensure that the accumulation is not eroded or adversely impacted by loans, in-service withdrawals or excessive fees. Although this focus remains, the employee benefits community is also concerned and considering the regulatory framework relating to the distribution of retirement income. I am pleased to speak to you today about how that regulatory framework should be designed so that the assets employees accumulate can be secure during retirement. I will comment on all five issues that are the subject of this hearing. My comments on the first three issues are closely related and as such I will combine them.

These issues involve 1) addressing participant concerns about the risk of insure insolvency, inflation and premature death, 2) providing useful information to participants, and 3) furnishing participants with estimates of the size of their monthly benefits if their account balance were paid in the form of a monthly lifetime income.

Major employers like Honeywell do sponsor a variety of DV and DC plans. As I am sure you are aware, in recent years, a number of large employers have announced the closing or freezing of their DV plans to new participants. There are strong indications nationally that the percentage of employees who derive all or substantially all of their

employer retirement benefits will be from DC plans. Under most private sector employer-sponsored DC plans, the default distribution is a lump sum and the overwhelming majority of DC plans do not offer installments or annuities as a distribution options. ERIC members report that nearly all participants in the DC plans who have distribution options other than a lump sum do not choose that other option. Retirees who take their benefits in a lump sum may overspend and outlive their retirement savings. They may spend too little and live too frugally.

Without a doubt, a growing body of research suggests that employees, our future retirees would be well advised to address these risks by including one or more annuities contracts in their investment portfolio. The mismatch between the academic research and employee behavior may be attributable to the lack of information and understanding. Many employees don't understand what annuities are, that they might be helpful, or what they are paying for. They believe they are too costly, risky, vulnerable to inflation and a poor investment if the annuitant dies early. Many are also unsure of where to go for reliable information. Major employers like Honeywell would like to help employees, but we are concerned that any assistance that provide education will expose them to fiduciary liability under ERISA, that no good deed will go unpunished.

We have some concrete suggestions on how to address these concerns. The agencies should embark on an educational initiative to acquaint employees and retirees with 1) the potential risks and benefits of investing in annuity contracts, 2) to compare contracts and how to compare annuity contracts with other self-funding options, 3) how to evaluate an insurer's financial condition and how to evaluate state guarantee associations, and 4) how to obtain more information about annuity contracts. The agencies should partner with the department of education to undertake a major initiative, starting with our students to improvise the financial literacy of the nation's workforce. Although it might not be realistic to expect students and younger workers to focus on retirement, these issues must start early in order to maximize its effectiveness.

Many employees and retirees are accustomed to receiving useful, accurate and unbiased information from their current or former employers. The Labor Department should make clear that employers can educate their employees and

retirees about distribution options without being threatened with fiduciary liability and exposing themselves to litigation or penalties. Interpretive Bill to 96-1 regarding investment education is a precedent that the department should follow in regard to distribution education. Helping employees to estimate the size of annuity that can be purchased with their account balance could be useful. As long as the employees are cautioned appropriately about the uncertainties associated with estimates, there is no reason to require every plan administrator to prepare such estimates on their own. Indeed, most plan sponsors would be wary of doing so.

Instead, the agencies should establish a website that allows individuals to make such estimates after inputting key assumptions such as the size of the account balance, interest rate, age, and annuity commencement date. If contrary to ERIC's recommendation an annuity estimate were required to be included in each participant's account statement, generic examples should suffice. Plan administrators cannot be reasonably required to provide individualized estimates based on volatile and unpredictable factors such as the size of the participant's account balance and annuity participation rates at an uncertain future date.

The fourth issue relates to changes in the Labor Department regulation regarding the selection of annuity providers to make distributions from DC plans. The department has characterized its regulation as a safe harbor. It is not. Under the regulation a fiduciary selection of an annuity provider satisfies the duty of prudence only if the fiduciary engages an objective, thorough, and analytic search, appropriately considers information that is sufficient to assess the annuity provider's ability to make all future payments, appropriately considers the cost of the contract in relation to the benefits and services to be provided, appropriately concludes at the time of the selection that the annuity provider is financially able to make all future payment, and if necessary, consults with experts. The department's regulation is not a safe harbor. It does not provide that the law will be considered satisfied if specific objective steps are taken. It is laced with critical but vague terms that require subjective judgments. The DOL should establish a genuine safe harbor based on objective and universally applicable criteria such as the approval by an independent fiduciary that meets

criteria specified by the Department of Labor or by an agency that is approved by the Department of Labor.

The fifth issue relates to in-plan and out-of-plan lifetime income distribution options. Experience has shown that offering in-plan annuity distribution options is not attractive to employees and simply doesn't work. ERIC's members report that when a DB plan offers a lump sum option to retirees, a vast majority of them do not select it. This is true even though the annuity is the default option and even though married participants need spousal consent in order to elect a lump sum. This DB experience is quite persuasive. The DB experience indicates that requiring DC plans to offer annuity distribution options would be pointless and costly exercise, and for many employers, yet another disincentive to offering a plan.

By contrast, it remains appropriate to permit the distribution of DC plan assets to be in the form of a lump sum and to the extent retirees choose to have their benefits in the form of an annuity, to permit the retirees to roll their lump sum into a vehicle outside of the employer sponsored plan that supports a lifetime stream of income. DC plans that rely on an out-of-plan distribution option offered by insurers, mutual funds, or other financial institutions, have chosen, in effect, to assign responsibility for the design and marketing of distribution options to firms that are in the business of designing and marketing such products. This is an entirely sensible approach in my judgment, and it should be encouraged.

This concludes my prepared remarks, and I will be happy to answer any questions that the panel may have. Thank you.

Kevin Hanney:

My name is Kevin Hanney. I'm here representing myself, today. I am employed as an investment professional, and I have responsibility for overseeing large defined contribution plan based here in the U.S. and multiple defined benefit and defined contribution plans outside of the United States. My employer's large multinational based in the Northeast.

I'd like to take my allotted time this morning to talk to you about two of the general areas of interest that were in your announcement. But to put it more accurately, I'd

actually like to spend hours talking with you about everything related to lifetime income. I think the issue is that important and is that timely. Before I get into any details I'd like to just put some context around this. I will submit the full written statement but in the interest of time, I'll try to make this brief.

The world experienced an unprecedented financial crisis in these last few years. Powerful market forces stressed and then broke much of the financial infrastructure that had been in place for decades. The initial efforts of key individuals and their staffs both here and abroad eventually led to the support of virtually every major body in the world responding with previously unimaginable degrees of monetary and fiscal stimulus to staunch the torrent of economic bleeding. Sadly, this rescue effort happened only after the destruction of trillions of dollars in wealth. We're now at the beginning of a long and painful recovery period for most of the world's economy and the people, the lives, the standard of living that it represents.

Stop and consider for a moment, though, that all this happened at a time when much of the retirement income in this country is still supported by an infrastructure capable of financing it. Whether it's cash from the operations of a private enterprise or successful debt issuance, sources -- so just stop for a moment and consider that this all happened while defined benefit and Social Security was still as material piece of the retirement income that most American retirees enjoy today. Can you imagine what would have happened to today's retired Americans if their primary source of income was their finite savings held in their IRAs and DC plans? Let me take a shot at it.

First, the assets that generate that income and the standard of living it could support would've been cut virtually in half. Recent retirees would have seen the ability to meet their spending needs throughout retirement plummet as many of them shifted the consumption of their savings forward to maintain their accustomed standard of living. Some would clamor to secure an increasingly popular feature of retirement today. It's called the retirement job. But many would find themselves unable to secure employment in today's tight labor market. Overtime -- [coughs] -- excuse me -- overtime, retirees would adjust

to a lower standard of living but their impaired asset base would have the material impact on their consumption decisions for the rest of their lives. And finally, a senior retirees, when spending is focused far more acutely on healthcare and the preservation of life, we would see their mortality rate spike. This is a very serious thing that happened, and we're lucky that it happened now and not 15 or 20 years from now when there's possibly virtually no DV plans actively in this country.

The financial crisis that we experienced was profound. However, many retirees in the United States would have encountered far more devastating personal catastrophes if the support that they have today did not exist.

So let me pause here and say, though, I do not advocate reviving the era of the defined benefit plan. It will be difficult enough in the future to meet defined benefit obligations that exist today in the face of new accounting rules and an increased global competition. The direction we are headed where defined contribution plans and IRAs represent the primary source of income is likely the only sustainable path we can follow. However, that is not to say that we should not seek to preserve some of the best features of defined benefit plans. In fact, in order for the shift to be successful, it will be necessary to preserve the best features of both defined benefit and defined contribution plans. I believe the agencies are taking the right steps as evidenced by this hearing and the RFI, and I encourage you to continue to work to establish an environment which promotes and facilitates sufficient savings, appropriate investment and the establishment of reliable streams of retirement income. It's my hope that I can provide some comments today to assist you in that effort.

What I'd like to do is shift gears slightly now and make some recommendations for things that the Treasury might be able to do. First and foremost, a recommendation for new debt issuance specifically for U.S. based investors. A recent op-ed by Ralph Goldsticker, CFA, a managing director at BNY Mellon Asset Management proposed the creation of the new investment vehicle to address the problem of inflation protection retirement. 30 year amortizing tips, or A-tips [spelled phonetically]. I have permission to provide copies of the op-ed to agencies and included a graph to help illustrate how these instruments -- instruments might

work in practice. I borrowed heavily from his work to provide a description here.

A-tips would be similar to existing tips in that they are issued by the Treasury and provide an inflation adjusted rate of return. The difference is that rather than paying interest only to a majority, the A-tips would provide a stream of payments for 30 years that are constant in inflation adjusted terms. Each payment from A-tips would include both interest and a portion of the principal. The A-tips, if structured properly, would let retirees know exactly how much they could spend each year in inflation adjustment terms over the 30 year life of the security. After 30 years, the investment would not provide any more income because its value would be fully exhausted.

A-tips would offer many benefits in contrast to annuities. Payments would be guaranteed by the U.S. government. They would be constant in inflation adjustment terms. An active secondary market would likely develop given the desire of many investors to hedge their inflation exposure. Insurance companies that wish to offer inflation adjustment products would be a natural source of demand. As with other treasuries, A-tips would be inexpensive to trade and highly liquid. As a result, if the investor's circumstances changed -- and I'm talking about individuals here -- it would be fairly straight forward and inexpensive to adjust or liquidate a portion of the portfolio and pricing would be determined by the market.

Second suggestion that I would like to make is really more a series of questions as it relates to the Treasury Direct platform. Why isn't this system more widely advertised to the general public? Current evaluation yields aside, in general, isn't it a good idea for Americans to hold our own debt? Through Treasury Direct I have the opportunity to schedule periodic automatic debits from my bank account in return for which I receive certificates of indebtedness issued by the Treasury. These certificates remain in my T Direct account until the next auction of the issue I wish to purchase. At that time, purchases are made through noncompetitive bids and can be made in increments as small as \$100. This entire process is free of charge for balances with less than \$100,000 in principal, and even at that point, a flat administrative fee of \$100 is charged annually. Why isn't this available to every IRA and DC plan in the country? I believe there is already a facility

to set up direct payroll deposit through Treasury Direct. This should be a standard feature of every DC plan record-keeping system, up to the plan sponsor to whether they introduce it or not but the functionality should be there.

Furthermore, why doesn't Treasury Direct offer IRA and ROTH IRA accounts or at least their analogues? The nature of inflation adjustments and traditional tips make them very inefficient to buy and hold in a taxable account. Establishing analogues of ROTH-IRAs and IRAs directly through the platform would be very advantageous for individual retirement account investors.

In the time remaining, I'd like to make some comments about the safe harbor, but I don't believe that I'll actually get through all of my pages on this so feel free to cut me off. Ambiguity and the current guidance: I sincerely appreciate the DOL's effort to provide this guidance. Its existence made things considerably easier for me and colleagues in recent years as we promoted development of lifetime income solutions. However, I'm not sure who, if anyone, has actually called the DOL to find out exactly what it means. I can tell you, I've seen widespread misunderstanding, misinformation, and plan old ignorance regarding the rule and its implications. About the only thing I can say I have not seen is broad misapplication of the rules, and that's because most people who would be in the position to apply it have so many questions and concerns that many believe it's not even worth it to try. A lot of plans are waiting to see who will take the first step in the hope that they will learn from others' mistakes.

There are numerous questions one might ask. For example, how do you defy the word annuity? Is lifetime income vehicle an interchangeable term? Distribution options come in many forms. Are you including all forms of options or is it just limited to products backed by life insurance companies with embedded guarantees? We need to know. Plan sponsors need to know because in addition to traditional annuities, they're looking closely at guaranteed lifetime withdrawal benefits. They're also thinking about products that are not directly backed by insurance companies at all, such as [unintelligible] tips portfolios or nominal Treasury portfolios which are only supplemented by deferred annuities as longevity insurance. Some might elect to forgo the annuities entirely and just go with laddered government securities. This is arguably the lowest risk

and lowest cost way to implement a program of U.S. dollar based lifetime income.

But it leads to another question. Does the safe harbor guidance only apply to income backed by entities with state insurance charters? And if so, are some charters more equal than others due to differences in the state's standards? Is the operative characteristic at issue here whether or not the entire value of the lifetime income ultimately eligible for coverage under a state-guarantee association? If that's the case, we might run into serious problems regarding the extent of coverage because the GAS [spelled phonetically] in most states only guarantee \$100,000 to \$300,000 of coverage. That is not enough to keep people in the standard of living that they've grown accustomed to in many cases.

[chime noise]

Thank you for the time, and I appreciate your questions.

[laughter]

Male Speaker:
Want me to start?

Male Speaker:
Yeah.

Male Speaker:
Thank you for your testimony. I'd like to start with one question for Ms. Boyd. I understood you to say that participants at your company have an option of rolling an account balance into the defined benefit plan?

Janet Boyd:
That is correct.

Male Speaker:
I'm just curious. Have you looked how the level of income stream that that provides compares to with what would be available if they went into the annuity market?

Janet Boyd:
To be honest, we haven't done that at all. In -- for the most part, this particular aspect of our 401k plan, to be honest, hasn't been taken up that much. Of -- for example,

we usually have around 50 or 60 individuals that leave the company and are going into our retirement system on a monthly basis. And I would say about five to six or seven of them in any one month might take this as an option.

And most of the time, the individuals that do take the option are those individuals that, for whatever reasons, their DB plan balance -- and remember we have a balance, a system, either a PEP plan or a cash balance plan but most of our employees are still under the PEP plan. At any rate, in that case, if the balance is very low, that's when they're more likely to move the 401k balance over.

Male Speaker:
Thank you.

Male Speaker:
Thanks so much for your testimony. For the employer representatives, just curious, you all talked about the lack of a clear fiduciary safe harbor. Is it your sense that there are many employers out there that are poised to offer these types of products if given more of a clear safe harbor? Do you think that is the primary impediment with respect to the individuals that you're affiliated with?

Allison Klausner:
I think that that -- the fiduciary concern is a primary concern. It is a major obstacle right now for employers to consider doing it. There are other concerns, and I don't want to minimize them. One of them is the idea of revamping all of the systems. I mean, conceptually the idea of developing everything that's necessary to mimic a defined benefit world in terms of distribution options into the defined contribution world is a challenge and it is a costly undertaking.

David Wray:
I would say that the fiduciary issue is so daunting that it pretty much ends the conversation. I mean, if we really want to know how many people are interested we've got to solve the fiduciary issue first. Because what happens -- it's a wall. You go to people and say, "Gee we should do some innovative things with annuities," and the first question is, "Well, what's the fiduciary liability?" And they say, "Oh, my gosh, do I have to -- you know, is my company guaranteeing this payment for the next 35 years, and you know, are we going to be sued?" What is, I mean,

so it just stops the conversation. So, with -- without getting this problem -- get past this -- you're just not going to have that much interest. We've got to get this resolved.

Kevin Hanney:

I'd like to say that there are several large employers who have taken the leap and spent years looking very closely at these options. The ambiguity in the guidance is a bit of an obstacle, but there are certain plans that would like to see some clarity and once they get clarity I think what you'll see if rapid adoption. Probably among the larger plans because of the time and the resources they have available.

Janet Boyd:

And I would echo from Dow's perspective, we're pretty much in the same boat, but to be honest, until you get the fiduciary system in place or at least -- you know, having some sort of safe harbor, I don't think the market is going to develop enough. Right now we believe that the market is too expensive and too complex and a lot of that complexity and expensive nature of the market is due to the fact that the fiduciary responsibilities are not entirely clear. But you've got to deal with all aspects of it. We're not going to find ourselves in this situation in which we try to offer something and find out it's so complex that our employees don't either take advantage of it or we have to pull back.

Male Speaker:

Thank you. Ms. Klausner, you talked about what sounded like a recommendation for a fairly aggressive governmental education program including the Department of Labor, the Department of Education. First of all, is there a consensus among the panel that that kind of program is necessarily a governmental responsibility?

Janet Boyd:

That's a good question. To be honest, I hadn't really thought that through. Obviously, anything to improve the market is in our best interest, and if by providing support through website education opportunities perhaps that would be helpful but to be honest, I hadn't even thought about exactly how that would work. We're really focused on making sure that the market develops in such a way that we can take advantage of it.

David Wray:

We've been in favor of education at the school level for a long time. Our view is that the employer -- I mean, to look at the system and say that people who make cell phones and sell groceries should be responsible for teaching America's workers how to invest their money is a reach. It's wonderful that the employer community has stepped up, and the providers have supported, and we've spent all this money, but it's a very inefficient system and leaves a lot of people out. Adult education is very, very difficult, for any of you that have actually done it.

And so, I think, if we're really going to get our hands around how we manage money effectively over a 100-year lifetime, it has to start much earlier than when a person is, you know, taking their first job. I mean, so we would certainly support that -- you know, I think it probably needs to be a partnership of a whole bunch of people. It isn't just the government. But I think the -- and the government has started some initiatives in this area, but it's really a community of effort issue. And we all have -- we all benefit from this, and I think we would all participate. But just like we don't think it's a 100 percent government problem, we don't think it's a 100 percent employer problem, either.

Allison Klausner:

If I can add, that's a perfect ending. It's not something that the employers welcome, particularly when the employees come to us -- some, of course, very well educated, depending on the industry that they're in or the level of education that they had, but as we enter the world of trying to explain to them how a lifetime stream of income may or may not work under a variety of circumstances, we're still left with an employee population that greatly doesn't understand how to balance a checkbook, what simple interest rates mean. They still confuse very basic concepts to those of us who live in the retirement world, such as what's the difference between directing your future investments versus reallocating your current account balance. That concept alone, in terms of how to move their money or use their money while they're accumulating it, already trips up many employees around the nation.

So, if we start in the early years like we used to have shop or home ec or any of those basic life skills, I think

we need to see financial literacy as a life skill that if we start, you know, back in third grade when the employees get to our -- our workforces we will find that they are educable in this manner and that we will be successful as a nation.

Kevin Hanney:

I think the obstacle of education is almost insurmountable. I think that every individual in this country has a responsibility to take care of their own financial situation and they have a responsibility to educate themselves as much as possible. There certainly is a lot of information out there. The biggest problem, though, is that most of that information simply doesn't apply to individuals. Just simple concepts like risk, the rules of thumb that we use, the things that you hear on television, the commercials during halftime at a ballgame. A lot of that stuff just doesn't apply because as individuals we all live in a fat tail. You know, any one of us could step off the curb tomorrow and get hit by that bus or financial bus, whatever it might be. So if we start to try to apply some things like the concepts of modern portfolio theory that have some very stringent assumptions that are pretty much violated by regular everyday types of events. We're probably going to underestimate our risk and we're probably going to overestimate our return possibilities.

So, I think it is critical for us to try and educate individuals, but at the same time, it's very important to try to create a system that has all of the freedom in the world for people to make bad decisions but to give people guidance as to what the most likely, appropriate decision would be for somebody given their circumstances. So, if you can put sort of those bumpers on, those training wheels, and when people want to take 'em off, they've got the freedom to do that, you'll be successful. But I don't think that education's quite going to get us there on its own.

Male Speaker:

Thank you. When you talked about fat tail I was thinking about my exercise regimen I'm actually trying [inaudible] -
-

[laughter]

Kevin Hanney:

Mine's in my seat right now.

[laughter]

Male Speaker:

But, I think David, you mentioned portability and obviously that's one of the systemic challenges. I'm just curious from the panel, Ms. Klausner, maybe you could comment on the issue so you'd share the Lifetime Income Committee within ERIC. Any thoughts on portability? That's obviously one of the big challenges that we have to think through.

Allison Klausner:

We have discussed it in the task force and with regard to portability, that it is one of the reasons why we are very interested in having the government and the industry pursue lifetime income streams outside of the plan. That's not to say that we've closed our minds at all to the possibility of in the plan but the concept of being able to take your lump sum and either bring it to a new employer, a new IRA, or some form of a lifetime stream of income that's provided through an outside financial provider whether it be a mutual fund or other. So portability is a great concern, particularly as our workforce today changes jobs many times more than the generations before us.

Robert Doyle:

Just to return to the safe harbor discussion for a moment. And without attempting to address the many good questions Mr. Hanney put on the table for us to think about in terms of the scope of that guidance, I'm sensing that probably the biggest challenge as it relates the safe harbor and perhaps we'll acknowledge that it's not a safe harbor in the traditional sense. It is an operative framework, kind of expectation in terms of the analysis that a fiduciary would go through in making a selection of an annuity provider. But I'm assuming that the challenge relates to the financial solvency of the issuer and is that the biggest concern in terms of the safe harbor? It's not the necessarily the quality of the product or provider or the cost of the product that presents the challenges for the fiduciary.

Kevin Hanney:

Can I take a shot at that?

Robert Doyle:
Sure.

Kevin Hanney:

I think the solvency issue is clearly one of the most important and difficult things to get your arms around and when you read through the comments that came out around the announcement of that final guidance or the final rule, there are references made to ratings agencies, and it's suggested while it's not part of the final rule, that plan sponsors may find that information helpful and it is to some degree. You know, I actually have a copy of the AM best financial rating methodology that I'm reading through and trying to understand as deeply as possible. But the reality is that ratings agencies have repeatedly missed risk on a wide scale and what I'm not sure, as somebody who may or may not be able to rely on what's been issued by the department is, can I rely, am I entitled to rely on a rating?

If I think about just the states of receivership that an insurance company can go into, there are three general states: there's conservatorship, there's rehabilitation and there's insolvency. If a state insurance commissioner has any concerns about that insurer not being able to pay their future claims, they're going to go into conservatorship, they're going to go into rehabilitation eventually and if they can't fix the problems, they will go into insolvency and then the state guarantee association's going to get involved. There might be an assumption reinsurance deal worked out. Other insurers in that state who are in the same line of business will basically hive off the book and take it over. Or in some cases, you might have an extended run-off where the state guarantee association essentially levees all of the insurers who are in that same line of business and pays those claims as they come due. I think Executive Life is one of the few examples we have of that happening. The reality is there are not many precedents for these things actually happening in the states. Back in the early '90s, we had some blowups.

So from my perspective as somebody who would be potentially making the selection of an insurer, and following due process and doing my best to understand is it a static hedging model, is it dynamic hedging model, how many Greeks are being hedged? Are we doing vega [spelled phonetically], delta [spelled phonetically]? You know,

tell me what you're doing from the ground up. But does the safe harbor provide sufficient confidence to me that my process is what will be evaluated, not necessarily if I have the appropriate conclusion. Because the reality is, the state insurance commissions probably know more about these insurance companies than I ever will. And at times, they have to get involved.

Robert Doyle:

Yeah and I think at least one of the commenters on the RFI suggested a standard whereby, you know you -- the fiduciary should be able to rely on a company that's licensed in multiple states, for example, and as a basis for at least getting past the solvency aspect and I'm curious as to whether you have any reaction to that type of standard?

David Wray:

Well, I mean, you know, as I said in my comments, I mean, what we have to have is the government has to stand behind us standing behind the decision. I mean, it's just about that straight forward. I mean, what you -- if -- what you're suggesting is if we pick a set of criteria for the provider that provides the annuity, that means that we absolutely 100 percent can rely upon that in every way, and the question is, is the government going to stand behind that? Because if the annuity stream is -- we just heard a very complex process, and I was involved in one of those things and took 10 years to fully take care of all the issues and there was an interruption during that process. Okay. So, if there's even -- if they start down that path, you know, there -- are the annuities going to continue to get paid, I mean, how is this going to work? I mean, there has to be confidence that somebody is going to make sure that those annuity payments are going to keep running and it's not going to be a responsibility of the employer who relied upon whatever criteria it is that the government set.

I mean, so you know, we're looking for very specific, you know, criteria, that we can rely on 100 percent and that nobody is ever going to be -- because if one of these programs goes down, the political fallout is going to be significant. So I just, I mean, it's a serious issue. It's a tough one to --

Robert Doyle:

Well, I mean, one of the things that we articulated in the safe harbor was that the expectation at least of the department was that the judgment would be made at the time of the annuity purchase. We wouldn't be -- it wasn't a look-back rule, that, you know, in the event of insolvency or failure later that that's the standard that's applied. But I've not gotten the impression that -- I'm not hearing a lot of confidence in that being the standard that's actually applied.

Male Speaker:
[unintelligible] be that forgiving.

David Wray:
I mean your --

Allison Klausner:
That's-- right.

David Wray:
Please.

Allison Klausner:
One of the other things is how often do we do this? If there is a safe harbor, and it's concrete, if it has, you know, certain standards by rating agencies one through three. If it's been in existence or licensed in certain states, you know, times 10. You know, we can have objective -- and then we select one or two or three potential annuity providers, do we review that weekly, monthly, yearly? So that as the next bunch of individuals who retire and want to select an annuity that we have, we can rely upon the annuity provider we picked two years ago, three years ago, four years ago? I mean, clearly, in the investment world, as we provide investment options, under our 401k and other defined contribution plans, we have a committee that's in place, and I'm sure many employers do as well that not only do we meet perhaps quarterly but we are on -- those that are on the committee are on standby at any time that a manager calls and says that there's a change or any time that the financial landscape out there begins to shift or change sometimes quickly and unexpectedly and at other times, gradually. We have that responsibility, and it's a huge fiduciary responsibility that we take very seriously, and I'm sure all employers do. The question is, even once we have an objective criteria for picking an annuity provider for a distribution, are we

done? What's our obligation to go back regularly to review as to whether that annuity selection is a good one?

Kevin Hanney:

I have a lot of experience with insurance companies in the stable value context. And we understand them pretty well, at least we believe we do and in the fall of 2008 when things started to get quite hairy, we were watching the Bloomberg terminal on an hourly basis, looking at credit default swaps spreads [spelled phonetically], getting a sense of what's happening to the common equity as some of these shares literally fell to very low values.

It -- from an investment perspective and from an on-going concern perspective, there's certainly a feeling out there that I hear from people that I talk -- talk with this about that there is an ongoing requirement to oversee those insurance companies. However, given the safety net that exists, and if we are entitled to rely on that, what are the circumstances that would ever trigger us to actually pull away from a benefit that could potentially be paid in the future because these participants will be paying. They'll be paying good money to get that benefit and it's hard to envision a situation except perhaps in the [chime] in the extended run off where there is an interruption in payments where you were literally want to pull that benefit. And I think that it would be very helpful if the department or the agency could provide some guidance with regard to that. Because I think that's sort of the ultimate question -- when it comes to an investment manager, it might take some time. We might need to see some evidence but we can replace the -- the investment managers. With an insurance company and this lifetime benefit, it's a lot more permanent.

Robert Doyle:

If there are no more questions, I'd like to thank the panel.

Female Speaker:

Thank you.

Female Speaker:

Thank you very much.

Panel Two

Robert Doyle:
Good morning.

Karin Feldman:
Morning.

Josh Shapiro:
Good morning.

Karin Feldman:
So, following your suggestion on the first panel, plus Josh and I flipped and we decided to use that order. Good morning, I'm Karin Feldman from the AFL-CIO and we thank you for the opportunity to present our views this morning on two of the issues -- two of the five issues that were raised in the hearing notice: participant concerns affecting the choice of lifetime income options and the disclosure of account balances as a monthly stream.

The AFL-CIO and its 57 affiliated unions, together with its community affiliate, Working America, represent more than 11 million workers across our country. These workers are throughout our economy in both the private sector and all levels of the public sector, state, local, and federal. And these workers participate in a wide range of pension and savings plans: defined benefit plans, both single and multi-employer, traditional, hybrid, as well as defined contribution plans, including 401k savings plans.

In our view, defined benefit plans remain the most sound and cost-effective vehicles for building and safe guarding retirement income. They use professional asset managers, they offer lower investment fees combined with better returns, and most importantly, they offer a stable, steady, lifetime monthly income. The majority of represented workers in the private sector, according to the Department of Labor, 68 percent participate in defined benefit plans today while those who are not represented, only 16 percent have that coverage. But as was pointed out at the opening of today's hearing, the landscape has obviously changed. The erosion of secure defined benefit plans and the explosion of cheaper, less secure defined-contribution plans has expose severed deficiencies in our current retirement system, particularly, with the decline in asset markets, a process that began just two years ago and is

imperiling the savings of workers as well as the funding of defined benefit pension plans.

We welcome a national conversation, a dialogue as everybody said this morning in opening, but we also believe our conversation needs to be broader than lifetime retirement income and how to annuitize benefits from 401k savings plans. We need to have a serious conversation about retirement security. There are too many workers without any coverage, too many workers with stagnant incomes who can't afford to save for retirement, and too many employers who abandon pension plans for 401k plans or no plans at all. We need to do more than tinker with existing savings plans, offer automatic enrollment in IRAs or encourage the inclusion and selection of lifetime income options. We really need to develop and have a serious conversation about a new system for providing universal coverage and adequate, steady, lifetime retirement income.

One initiative of which the AFL-CIO is part, Retirement U.S.A., has outlined a number of principals that would guide that national conversation that we really think needs to happen, and we hope that this discussion, it might be the beginning of that broader dialogue.

And while we've pointed out, our view that lifetime benefit payments are critical and offer a security to retirees and their families, particularly offering them through defined benefit plans which allows these risks to be pooled over larger groups and over generations of workers and retirees are useful, we know, as was pointed out this morning, that many workers elect lump sum distributions if they have that choice under a defined benefit plan and then, in addition, 401k savings plans generally provide only one payment form, a lump sum distribution.

The concerns that we've heard from our affiliates, at least with respect to the choices of taking single sum distributions from defined benefit plans, one is a concern about the future. Many of the folks in industries undergoing consolidation and restructuring saw their fellow workers that other employers lose benefits in large part as a result of the limits of the guarantees provided by the pension benefit guarantee corporation. For others, it's the possibility of a significant payment. They don't connect the value of the steady monthly lifetime payment and compared to the present value of the lifetime benefit

which they see as a large single sum of money. They've never seen anything like that before, and it could be used to meet other pressing financial needs, especially in today's environment.

On the other hand, while there can be large balances in 401k savings plans, right now for most workers, those balances are relatively modest. One study showed as of June 2009, the median account balance in a workplace plan was around \$70,000 dollars for workers close to retirement, age 55 to 64. And this balance provides a very small monthly payment of around \$400 for the worker and his spouse.

So, on the one hand while there's the temptation to take the large sum because the present value of the defined benefit lifetime stream, on the other hand, if you have a small balance in a defined contribution plan, it may not seem worthwhile to annuitize it, assuming that you know how to get that information or have it easily available. Because those participants considering lifetime income payments out of the defined contribution plan must make the extra effort, essentially, in today's world to seek outside advice and information and face the likelihood of additional fees, both in obtaining that advice and in purchasing an annuity in the retail market.

All of that suggests the possibility that it might be worthwhile to include lifetime income options within defined contribution plans. However, we have some concerns about doing that without significant changes in today's market because I think without those changes, that it's less -- it's unlikely that workers will choose to purchase annuities and while we may not agree with the employers who spoke earlier, employer representatives who spoke earlier about the utility of the department's safe harbor, we think it's worthwhile that they consider including these options in plans.

And part of that will help make people more familiar, I think, with annuities, how they work, and that's another aspect that the education that could come with the disclosure of account balances as a monthly income stream, they're closely related, I think. For the most part, over the last decade, our conversations on retirement security have been emphasizing the responsibility of workers and their families to save and fund their own retirement. The

focus is on the next statement and the account balance that shows. Is it up? Is it down? Do I change my investment allocations? Is there another option available, one providing a better return? The whole -- to some degree, this emphasis on accumulation and really short-term returns and outcomes overshadows the ultimate purpose of that account balance, the provision of income during retirement.

In our view, including, at least on one statement a year, the monthly lifetime balance together with the account balance can be a useful tool in teaching participants the ultimate value of their accrued savings. While it may not be enough, standing alone, to change the ultimate distribution decision at retirement, we think providing the illustration of the monthly benefit over a series of benefit statements year after year may help encourage workers to consider all their options.

The monthly benefit on that statement should be at the plans normal retirement age and based on the accrued benefit as of the date of the particular statement. An appropriate long-term rate of return assumption, one consistent with investments typically available to 401k savings plan participants should be used and the annuity conversion based on commercially available rates. It could be useful as well, to include both single life and survivor annuities for married participants, again, as an illustration. And it's also comparable in many ways to the information that's provided to defined benefit plan participants to show the impact of making a decision one way or the other on a benefit option.

Protecting contributions to retirement age, in our view, introduces another complexity to any illustration, and it has the potential, we think, to mislead. Future contributions depend on a variety of factors. The decision to continue deferring compensation. The continued ability to work, whether due to health or economic conditions. Continued coverage under the same plan and, in many cases, continued employer contributions. Most importantly, including assumed contributions to retirement age could easily lead participants to believe they will have more funds available at retirement than might actually turn out to be the case.

We suggest that the department specify the assumptions to be used in these determinations; in part, because doing so

will ensure uniformity across plans and avoid unreasonable and inappropriate assumptions. It could also, in our view, moderate administrative cost and the concerns of the potential burden, as the employers have expressed some concern about, this morning.

In closing, I think the key to anything here is to recognize that the emphasis has to change, generally in our conversations about what -- what defined contribution plans are trying to do and what we are trying to -- what is important about retirement and retirement income. By focusing, as we have, on accumulation and lump sums and your balance, we're missing the boat, that the focus is what do you need to live on when you retire and how do you get there? Thank you.

Josh Shapiro:

Good morning. My name is Josh Shapiro. I'm with the National Coordinating Committee for Multiemployer Plans. The NCCMP is a nonprofit and nonpartisan organization that represents the interests of multiemployer pension and health and welfare plans. The majority of these plans are defined benefit plans that do not offer lump sum payments. As such, the subject of this hearing is not directly applicable to most of the plans that we represent. However, over the past few decades there has been a steady movement in other sectors of the retirement industry away from plans that primarily pay benefits as annuities and towards plans that primarily pay benefits as lump sums. We consider this to be a very unfortunate and dangerous trend as benefits paid as annuities are vastly superior to lump sum payments in providing retirement income security to participants. While this trend has not yet affected a substantial number of our plans, we are part of the wider retirement system in America and the deterioration of the effectiveness of this system necessarily has an impact on the ability of our plans to survive.

While it may sound obvious, it is worth stating that the primary purpose of any retirement plan is to provide a retirement income. Many retirement plans these days serve other purposes. However, the importance of providing retirement income must outweigh all of these other concerns. With this fact in mind, it is impossible to argue that a lump sum payment is a more effective vehicle for providing retirement income than annuity payment.

Participants who attempt to fund their retirements with single sum payments must decide how long they will live in retirement and what their pattern of expenses will be. Some will inevitably drive down the payment too quickly, leaving them with no income from the plan for the latter stage of their retirement, while others will be cautious, living far below their reasonable means when they could have maintained a higher standard of living in retirement.

Proponents of lump sum payments will point to the participant who passes away shortly after he retires, claiming that this individual will have received a very poor annuity benefit compared to an individual who lived for decades in retirement. However, if we focus on the primary purpose of retirement plans, we see that both of these individuals received really the same benefit. Each received reliable income throughout their retirement. As long as the size of the benefit was appropriate, neither individual had to spend a moment worrying about how they would find the money to pay their electricity bill, how they would afford their healthcare expenses or how they would afford presents for their grandchildren. Retirement income is all about security which is measured in piece of mind, not in dollars.

Despite these advantages, in instances where participants have the ability to choose between a lump sum distribution and an annuity, the overwhelming majority of participants select lump sums. While we do not have detailed survey data in this era, we are not aware of a single plan where the percentage of participants taking lump sums is below 90 percent and over 95 percent is common.

There have been many proposals out there for encouraging participants to take more of their benefits as annuities. Some of these are providing more resources and services to better educate participants. This could possibly be coupled with a communications campaign to make participants more aware of the benefits of annuities. Additionally, steps could be taken to improve the pricing of annuities in the retail market. Another idea is to provide tax advantages that would apply to benefits taken as annuities. We consider all of these to be worthwhile ideas; however, we do not believe that any of them will substantially alter the current pattern of elections. The fact is a lump sum payment simply feels much more valuable to participants than does an annuity of equivalent value.

For example, using reasonable [unintelligible] assumptions, a lump sum of \$100,000 payable to a participant at age 60 is worth somewhere in the neighborhood of \$550 per month. It is unlikely that any amount of education, communication or incentive will convince the average person to pass up \$100,000 in exchange for \$550 a month even though they are equivalent.

The single most effective way to reverse this trend would be to encourage new growth among defined benefit plans. Since these plans calculate benefits as annuities rather than as single sums and those annuities are paid directly out of plan assets, there is no issue with unfavorable annuity pricing. In the early days of ERISA, receiving annuity benefits from retirement plans was nearly always compulsory as plans were defined benefit and very few of them offered lump sum options. However, with the growth of cash balance plans in recent years, and the migration towards defined contribution plans, the situation today is very different.

However, we are also realistic in that we recognize that any return to defined benefit plans would meet substantial resistance from the business community. There is a widespread perception that these plans are too expensive and too risky for businesses to sponsor. The reality is that, relative to defined contribution plans, defined benefit plans are inexpensive, and there are highly effective techniques to mitigate or eliminate the risk of these plans. However, this discussion goes beyond the scope of this testimony. So, for now, we will simply accept that any meaningful return to defined benefit plans is unlikely in the short term.

Accepting that defined contribution plans are here to stay, the challenge becomes how to structure these plans so that participants will receive their benefits as annuities. For the reasons discussed earlier, we do not believe that there is any way to substantially shift the pattern toward annuity payments without making annuity distributions compulsory. While we believe it is permissible for defined contribution plans to do this under current law, very, very few plans have done so. We encourage the federal agencies to work to create an environment in which plan sponsors will be comfortable adopting mandatory annuitization of defined contribution balances.

Mandatory annuitization does create some special issues in defined contribution plans. In many cases, a substantial portion, if not the majority of the participant's total balance comes from elective deferrals rather than employer contributions. This money is more a form of individual savings than an employer-sponsored retirement income. As such, it would be inappropriate to prevent participants from taking lump sums on this portion of their balances. Our suggestion of mandatory annuitization applies only to employer sponsored contributions, looking primarily at matching contributions and profit sharing contributions. Additionally, we would not suggest that this apply to current balances. Our suggestion is that this change to mandatory annuitization would apply only perceptively to future profit sharing and matching contributions in defined contribution plans.

Paying annuities necessarily involves the sharing of mortality risk across a population of individuals. This is actually what makes them so great. However, in the defined contribution world, each individual's balance is segregated from all the other employee's balances which makes it very, very difficult to share mortality risk totally within the plan. It is far simpler to use the accumulative balances to purchase annuities from private insurance companies than it is to actually try to structure annuity payments from inside a defined contribution plan. I am aware that there have been several financial institutions that have tried to market those ideas in recent years and, to my knowledge, they've had very little success due to the complexity of such an attempt.

So currently, in most cases, when a participant in a defined contribution plan wishes to receive the benefit as annuity, he or she would first receive a lump sum distribution and then find an insurance company that would sell them an annuity for that distribution. However, this annuity is certain to be much smaller than reasonable, actual assumptions would dictate, given the size of the account balance. And one reason for this is the fact that the insurance companies know that people who purchase annuities tend to be in excellent health and so they will appraise the annuity with the assumption that the buyer will live an exceptionally long time. Basically, they realized that someone who's just had four heart attacks doesn't buy an annuity.

Additionally, the insurance company will build many costs into the pricing, such as marketing costs, administrative costs and underwriting costs and lastly, the insurance companies are businesses seeking profit like any other so the cost of the annuities will include a margin for profit. All of these reasons contribute to the fact that buying an annuity right now on the retail market is a very expensive proposition.

What's interesting is if a large number of defined contribution plans began to require mandatory annuitization, this would address several of these pricing issues automatically. For example, it would no longer be appropriate for the company to assume that the purchaser of the annuity was in exceptional health if all members of the plan were buying an annuity mandatorily. Also, the increase in the volume of purchases and the reduced need to market and underwrite them would contribute to lower expense figures. And lastly, the defined contribution plans themselves would become very large purchasers of annuities, which would provide negotiating leverage on obtaining the best prices.

Another option, should these insurance companies be unable to meet this demand, is for the government to enter the market directly. This would only be an option if it is determined that the insurance industry is unable to provide a large number of reasonably priced annuities for defined contribution plans. Depending upon how aggressively the agency priced these annuities, it could be done with little or no cost to the taxpayers. It would purely be a benefit to the participants in these plans. Hypothetically, in this model, plans could still contract with private insurance companies but the presence of the government in the market would insure that there's adequate competition and that the participants receive fair pricing of their annuities. We would certainly suggest that government participation be limited to the annuitization of defined contribution accounts. It would not be available on the wider market.

In conclusion, we believe that employer-sponsored retirement income should be available to participants only as annuities. Paying these benefits as single sum amounts is contrary to the principals of retirement income security

and will ultimately lead to a poverty crisis amongst older Americans. Thank you for your time.

[low audio]

Male Speaker:

I have one question. Both the previous panel and this panel has spoken a lot about the desirability of showing participants what they're account balance translates into as an annuity stream in retirement. And Ms. Feldman was pretty specific about that conversion from the current balance projected forward based on a reasonable rate of return to some date of conversion to an annuity. I guess my main question is, should there be an attempt to be as real as possible in respect to what the balance could buy given existing market realities? Is that the goal? I mean, you can talk about, you know, what do we think is mortality and what do we think of the interest rates, but unless you address the adverse selection and loads and things that the other panelists talked about, what should be the target here? What are we aiming for in that disclosure?

Karin Feldman:

Yes. I think you probably do -- would want to be realistic, but I'm thinking as I begin saying that about you know how helpful are illustrations. One thought comes to mind that if you're not reflecting the market that's actually there for annuities, you're not really helping the participants and, again, the possibility of providing misleading information.

On the other hand, we've also heard -- we have a critique of the market and so how do you reflect a market that ought to change? Should you do it based on the possibility of group annuities because you want to encourage defined contribution plans to offer it so that that might have some changes in what the loads and other things are? I think the -- it cuts both ways. On the one hand, I think being realistic is helpful. On the other hand, I think it poses some additional complexities and probably doesn't make it particularly easy for plan sponsors to do without, you know, some good general guidance. And while we think it's a good educational tool and you had asked for, you know, concepts about what should be shown, we were trying to be responsive to that. So, Josh?

Josh Shapiro:

Well, I would say, I mean, if you are to do that, it would have to be, in my mind, as realistic as possible. I mean, one of the worst things you could do is to create an unrealistic expectation in the participant's mind of what they're going to get at retirement should they annuitize. You know, in our, you know, perfect world here where it's mandatory, it would be a realistic fact. You could actually say, "This is the annuity that we are purchasing for you on behalf of your balance," so it wouldn't have to be a hypothetical number but to the extent that's not the case, you know, I would say realism and conservatism would be important.

Robert Doyle:

Just any reaction to, kind of, the benefits as an alternative to a website calculator that participants could be directed true to input their own information and expectations?

Karin Feldman:

We have some concern about the -- you know, on-your-own environment generally. I think that those are helpful. Whether people will actually use them? Debatable. I mean, if you're going to -- if an employer is willing to adopt a plan, I mean, I think, yes. Having tools like that are good but I think people, especially in this area, where you're trying to maybe overcome concerns, sort of saying, here's your website, you know, go click, is probably less helpful than some solid material. And there may be a generational thing. I mean, I know I'm very tactile. I want the stuff in front of me and to hold onto it before I press that button. And Josh is a few years younger. He might feel differently.

[laughter]

Josh Shapiro:

I'm all for it.

[laughter]

You know, I think the more tools you can put at participants' disposal, the better. I mean, I would kind of go back to my concern that I don't think any amount of tools or education is really going to change what people are going to do. They're going to take the \$100,000. But,

you know, I'm still supportive of giving them more ability to at least do what they want to do, analysis wise.

Male Speaker:

I do just want to make sure -- and thanks for your testimonies, very compelling. To the extent that there was not a mandatory annuitization system, is it your view that the adoption rate would be so low even with clearer safe harbors, even with concerted efforts around education, that the adoption rate really would move in an appreciable way in a voluntary context?

Josh Shapiro:

Well, just to be clear, I mean, there's two levels of adoption. There's employers adopting this in their plans and then there's participants actually utilizing it. I'm not sure which of the two is the bigger barrier, to be honest. I would say probably participants. I think it is realistic that you could encourage employers to offer optional annuitization of benefits to participants. The safe harbor thing would have to be settled, of course, and they'd need some pushing, but it could be done. But I still don't think participants are going to take it. I think participants are going to take the lump sum. That's my kind of pretty strong view on the matter. I think -- speaking from my own point of view, and I've thought about this a lot, I'm not sure I could pass up \$100,000.

[laughter]

Josh Shapiro:

And I know as well -- I know as well as anybody, the benefits of the annuity and yet you put that in front of me, it's a tough thing to say no to. So if -- certainly, if I can't do it, I can't expect anybody else to do it.

Male Speaker:

For both of you, in the current world where defined contribution plans usually don't offer annuities, are you suggesting that the benefits statement of an equivalent in income terms be something that is facilitated by the regulators in the ways you've discussed. That is, by providing standard assumptions that plan sponsors could use or a calculator or the like. As opposed to suggesting that the plan sponsors be required to provide that kind of benefits statement. Previous witnesses in the previous panel, several of them made clear that they did not think

it would be constructive to require the income equivalent to be stated but rather to make it easier and more comfortable for sponsors to do that. Do you agree?

Karin Feldman:

No.

[laughter]

Did you expect another answer?

[laughter]

Again, I mean, I recognize -- while the plans themselves are not offering, at least today, meaningful access directly to lifetime income options, if part of what we're trying to do is get people to start thinking and look at things differently, I think -- and encourage them, if we can do it, despite Josh's concerns, it should be on the benefit statement, even if the plan doesn't do it. If it's all -- isn't that part of, like a holistic education program? I mean, if you're out there, on the one hand, saying, you know, "You need to think about this. Here's how you do it," you know, but on the very statement that you're getting of your account balance, there's nothing about it, it's a bit of a mixed message, I should think. So, yes, I think it should be required.

Josh Shapiro:

I think in terms of the role of the agencies, if I was a plan sponsor, I wouldn't do anything on this front, without some substantial involvement from the agencies. I mean, putting a benefit on a statement that's hypothetical -- in my experience -- terrifies employers, rightfully so. You've got future returns on there, you've got future pricing of annuities, you've got all this stuff, and one of employers' big fears is participants come back saying, "You told me I was going to get, you know, \$500 a month, or \$1,000 a month, and now I'm not." So, I think that for an employer to take any action there, there would need to be substantial guidance and involvement from the agencies, telling them just how to do it so that there's no discretion on their part they can be held accountable for in the future.

Male Speaker:

That kind of guidance or involvement that would give comfort to plan sponsors, obviously can be done in a way that does not require the plan sponsor to ---

Josh Shapiro:
Yes.

Male Speaker:
-- to use it.

Josh Shapiro:
[unintelligible] Second answer is yes. I would support the notion that should be required item on the statements, yes. So, I'm definitely, you know, with Karin there that if you're not going to have mandatory annuitization which obviously is what I think is ideal, I still think it would be a good idea in the current model, to require that it be shown as an annuity. Despite my pessimism, it may help.

Male Speaker:
One follow-up question: Mr. Shapiro, you've argued very strongly that you think annuitization should be mandatory. I guess my question is since we're talking, in many cases, about plans where the contributions are elective on the part of the participant and since you've said participants, when given a choice, choose lump sums, would mandatory annuitization have any implications for what participants decide about whether or how much to contribute?

Josh Shapiro:
Well, I certainly, and I hope this was clear, I would not apply mandatory annuitization to participant elective deferrals. It would only be the employer sponsored portion of the money. Just conceptually, in my own mind, I kind of separate out the money which the employer is putting in is sort of -- in my mind, that's the retirement plan. The money that the employee puts in, that's just savings. It's tax-efficient savings which is a good thing, but it's still it's their money that their saving. So, I would certainly limit the concept of mandatory annuitization to money which is paid directly from the employer in terms of either primarily profit-sharing and matching contributions.

[low audio]

Female Speaker:

I did just want to clarify, though. I understood you to say it -- it would not be a federal or a government requirement but that the employers would just design plans so that annuitization is mandatory. Is that --

Josh Shapiro:

In an ideal -- super ideal world I would say it could be a government requirement.

[laughter]

Returning to the world in which we live, I would say it would be enough to sort of try to encourage employers to voluntarily choose to design their plans this way. You know, again, I'm a realist. I don't think we'll ever get to the point where anybody will accept that's a requirement of the government, although I would like to see it. So, voluntary on the part of the employers but then it becomes mandatory on the part of the employees is how I'd phrase it. I hope that answers the question.

Robert Doyle:

Okay. Thank the -- thank the panel very much and thank you. With that, we will take a break until 11:15.

[break]

Panel Three

Robert Doyle:

Okay, thank you very much and with that, we will reconvene with panel three.

Jason Bortz:

Good morning. My name is Jason Bortz. I'm a partner at Davis and Harman, a Washington, D.C. law firm. I'm here as counsel to the Committee of Annuity Insurers. The Committee is a coalition of life insurance companies formed to participate in the development of federal policy with respect to annuities. Committee's current 31 member companies represent more than 80 percent of the annuity business in the United States and are among the largest issuers of annuity contracts to employment based plans and IRAs.

I wanted to start out by expressing the Committee's gratitude to the agencies for starting this project with the RFI and now, this hearing. The deaccumulation [spelled phonetically] phase of retirement just hasn't gotten the attention historically that it deserves, and I think the RFI and this hearing are a big step forward in terms of refocusing the retirement policy discussion in the right place and getting everybody to think about lifetime income.

I plan to spend some of my time today talking about the newer generation of life-contingent annuities. As you all know, too few retirees have the ability to annuitize through an employment based plan, and even when they have the opportunity to do so, too few folks are taking advantage of it. Insurers, however, have not been sitting by idle. They've been working to develop products that speak to perceived barriers to annuitization. And we believe some of these newer products have the potential really to result in higher rates of elections of lifetime income products. These next generation products really add options for managing longevity risk, in addition to your more traditional annuities, like a single premium, immediate annuity, which really continues to have an important place in the retirement system.

I think, at a fairly high level, our purpose here in talking about the newer products, is to make sure that you all as regulators have the information you need to first, think about how various reg projects work for annuities and

then to understand that annuities is a fairly broad concept these days, that it's not just the single premium immediate annuity. I think, as you all know, these issues have propped up in lots of the recent regulatory projects, whether it's the QDIA regulations where we work about how annuities fit into those products or, currently, the investment advice regular work, you know, in the Department of Labor for computer model based exemptions.

I'd like to talk about three kinds of annuity contracts that can fairly be described as next generation. This isn't a complete list of the products that are out there but they're some of the more prevalent ones and to be clear, you know, the products tend to work differently depending on the issuer. So we wanted to talk a little bit about in plan accumulation annuities, living benefits features, and then longevity insurance.

So, an in-plan accumulation annuity is an annuity that is offered as an investment option on a participant directed plan's investment menu, so typically offered next to mutual funds or collective investment trusts. It allows participants to allocate a portion of their contributions to the deferred annuity and to accumulate guaranteed pieces of retirement income. And because they're guaranteeing pieces of retirement income, participants are able to lock in interest and mortality tables. And get something that starts to approach dollar-cost averaging when they're buying annuities so they don't have this sort of point in time interest rate risk. Variations of these in plan accumulation annuities have been around for some time in the 403b market, but what's really new is the idea of including an accumulation annuity on a DC plan investment menu.

The other type -- the second type we wanted to talk a little about are living benefits features. So, this is a type of annuity that's been very popular in the retail and IRA space, and that's really starting to make in-roads into retirement plans. Living benefits come in a variety of forms, and they're available under both fixed and variable annuity contracts. One type is a guaranteed lifetime withdrawal benefit and the basic idea here is that the insurer issues a promise that wraps around an investment fund. It might be a balance fund or a target-date fund. And the promise is that regardless of the performance of the investment fund, or the longevity of the participant,

they're going to get payments for life equal to some specified amount. And the specified amount is generally based on something called the benefits base, sort of a notional account. It might be the high-water mark for the investment performance or it might be premiums plus some fixed interest rate. And so they have a guaranteed life time income.

A guaranteed lifetime withdrawal benefit can be imbedded in a deferred annuity contract or it can be issued on a stand-alone basis so that it wraps around other investments that are offered by third parties under the platform, so where the participant would only be buying the guaranteed lifetime withdrawal benefit.

Another type of living benefit that's making in-roads is a guaranteed minimum income benefit. Like the guaranteed lifetime withdrawal benefit, there's an insurance company promise that wraps around an investment fund, and here, the benefit's base will guarantee the participant the right to annuitize at a future date, say normal retirement age, using the greater of the actual investment fund value or the benefits base. So, it's a guaranteed base, generally protecting you against investment risk, prior to annuitization.

The third type of product that's proving to have some legs, here is a form contingent deferred annuity contract that does not begin payments until the owner reaches, generally, life expectancy. People refer to this as longevity insurance. Payments typically start at, say, at age 80 or age 85. And before reaching that date, there's typically very little in the way of cash value, and if any death benefit, there's only a very modest death benefit. And the idea is that, for a participant who lives beyond their expected life expectancy, they're going to be able to get a better deal on the annuity income that they get -- they'll get a better annuity purchase rate because of the risk pooling associated with folks who don't reach their expected life expectancy.

Unlike the other two -- in-plan accumulation annuities and living benefits features -- you don't really see longevity insurance in either IRAs or in employment based plans. The required minimum distribution rules effectively make it an impractical solution. And I think we'd like to see that

changed and to see longevity insurance be something that could be offered for IRAs and employment-based retirement plans.

Now, the responses to the RFI have a wealth of ideas about how to facilitate the use of lifetime income options, including these newer annuity products. And these range from revisiting the fiduciary safe harbor which we've already talked about, to expanding interpretative bulletin 96-1 to include investment education for distribution options and certainly this relief from the required minimum distribution rules. And the Committee thinks all of these are really good ideas.

We also think it's really important that you not lose sight of IRAs. There's incredible amount of money in the IRA space and lots of participants are going to take their retirement income out of IRAs so we'd encourage you to focus in part on IRAs and not just employment based plans.

Just very quickly we wanted to call out two sets of issues where some of these newer products had been raising problems and questions. One is portability. You know, if you are invested in a deferred annuity contract and you want to take a distribution from your plan, if the plan only offers cash distributions you may have to forgo valuable economic rights that are imbedded in the annuity contract or you have to leave the annuity contract behind. Insurers have generally dealt with this by providing for in-kind distributions of the annuity contracts, so they can be rolled over to an IRA custodial account or so that they can have an endorsement attached and become an IRA annuity. But the guidance in this area is really very thin, and we think it would be incredibly helpful if there was some clarifications around how portability works, how in-kind distribution works, and how you can flip to an IRA annuity.

We also think that there's one area where the law fundamentally presents an impediment. And that is where the spelled sponsor, plan fiduciary decides to eliminate the annuity contract investment option. There isn't really a system for completely eliminating that annuity and instead distributing it out to participants, really because of the restrictions in the tax law rules on in-service distributions. There's a system in the regs -- right now called the qualified plan distributed annuity contract where the insurer administers lots of the tax and ERISA

rules, joint-survivor annuity requirements, RMD rollover rules, and we'd like to see a system where the insurer could also administer the in-service withdrawal restriction, so that employers could get out of these contracts. And why do we want employers to be able to get out of the contracts? Because if they know they can get out, they're much more willing to step up and get into the contract. So we think that could be incredibly helpful.

The other one we wanted to touch on was spelled spousal consent. A lot of these deferred pay out annuities raise joint-survivor annuity challenges. And the basic problem is that they're two systems, the 401k system, where the spelled spouse only has the right to be the 100 percent death beneficiary, but doesn't have the right to joint-survivor annuity payments, the other, the defined benefit system, where they are only the 50 percent beneficiary, but have the right to spousal consent on distributions that are not in the form of a qualified joint-survivor annuity. When someone elects a life annuity, you shift between these systems. You go from the 401k model to this more defined benefit model, and we've got lots of questions about how those rules should work in there and all we really want are clear rules that we can administer so it's not an impediment to getting employers to offer these programs. So thank you very much, appreciate it.

Christine Marcks:

Good morning. My name is Christine Marcks, and I'm the president of Prudential Retirement, a business of Prudential financial. Prudential Retirement provides administrative plan-management investment and income products and services to planned sponsors and their plan participants, in the public, private, not-for-profit and governmental markets. We provide these products and services to over 6,500 retirement plans with about 3.6 million individual participants and annuitants representing over 180 billion in total account values as of the end of June. Today, what I'd like to do is share our views on American workers' growing need for guaranteed lifetime retirement income, and the importance of meeting that within the existing framework of employment-based retirement plans which is really core to our vision of redefining retirement for millions of workers and their families. I'd then be privileged to outline some recommendations on how to address that need through

specific regulatory guidance and clarifications that we believe are necessary to make this vision a reality.

Let me begin by providing some context for our recommendations. While guaranteed retirement income programs are currently available in the retirement plan marketplace, several impediments restrain planned sponsors from making these plans available and plan participants from electing them. First of all a guaranteed lifetime form of distribution within defined contribution plan is really a new concept for American workers. As you know, DC plans have replaced DB plans, and the primary workplace retirement vehicle for millions of American workers has changed. Unfortunately and unlike traditional pensions, most DC plans do not offer guaranteed lifetime income solutions. And among those organizations that do offer lifetime income options, many participants are reluctant to use their plan assets to elect and purchase one. Because DC plan accumulations are likely to be the largest amount of money, many workers even accumulate even a less than sizeable account balance can create an illusion of wealth, the mistaken impression that one will have enough to live on throughout their retirement years. This illusion causes many participants to underestimate, if they consider it at all, the need to purchase a solution that guarantees a stream of income that they cannot outlive. And even if the risk of outliving one's retirement savings is recognized and understood, many participants reject any solution that locks them into an irrevocable commitment or an inflexible payment strand. Finally, some participants may also fear the loss of a solution's full benefit that they or they -- that they or their beneficiaries will simply lose money if they die prematurely.

So, to respond to these concerns, insurers, including Prudential have created new forms -- and some of these were just mentioned -- new forms of guaranteed lifetime income solutions, such as guaranteed minimum withdrawal benefits or as we call them, GMWBs. GMWBs address participants' concerns by providing guaranteed lifetime income, but also providing access to one's account value at any time. They provide protection for retirement income against the risk of falling markets in the years preceding retirement alongside the potential to gain from rising markets. Participants have the flexibility to control their assets and the ability to include spelled spousal benefits as

well. A more thorough discussion of this product structure is included in our written submission.

I'd like to turn now to our recommendations. To facilitate a more favorable environment for guaranteed lifetime income solutions, employers and participants require greater clarity and guidance. As such, we have identified the following five areas that need the attention of the agencies.

First, modernize and update interpretive bulletin 96-1 to provide assurances to planned sponsors regarding the type of information and materials that can be provided to participants about guaranteed lifetime income without being considered investment advice. Second, issue guidance that encourages plan spelled sponsors to disclose annuity values in addition to lump sum values on participants' account statements. Third, clarify that the additional fees associated with guaranteed lifetime income solutions do not make these products per say imprudent for use as a qualified default investment alternative. Fourth, confirm the well-established principal that the prudence of a fiduciary's actions is judged on circumstances at the time an investment decision is made or reviewed, not in light of subsequent events. And finally, improve the annuities selection safe harbor for selection of lifetime income options. I'm going to devote most of my remaining time to that last point, providing details on improvements in safe harbor.

Our written testimony provides recommendations on these other items I've just noted. As I think you've heard already from some of the prior testimony, plan spelled sponsors find the availability of regulatory safe harbors to be very useful as they evaluate products and services. At the same time, they find the lack of a safe harbor or the lack of clarity about safe harbors in certain key areas to be a significant barrier in offering products and services within a plan. We recommend, therefore, that the department of labor issue guidance about the annuities selection safe harbor to clarify its application to guaranteed lifetime income solutions. We have three brief recommendations that are supported in more detail in the written testimony.

First, the department should explicitly extend the safe harbor and if necessary, appropriately modify it to include

a broad range of guaranteed lifetime income solutions. The fact that a particular guaranteed income solution is not a traditional, immediate annuity should not be a factor in deciding whether the safe harbor applies. The more important consideration is whether the solution appropriately protects participants against longevity and investment risks in a manner similar to a traditional distribution annuity.

Second, the department should also provide greater clarity about how frequently fiduciaries need to evaluate the financial strength of the provider of the guaranteed lifetime-income solution. We ask the Department of Labor to confirm that a fiduciary who evaluates the product provider's financial condition at the time the provider is initially selected must conduct subsequent reviews. When conducting these ongoing reviews, the fiduciary should evaluate the same factors used for initial consideration and at a frequency appropriate to existing circumstances, but no less than once a year.

Third, we believe the department of labor should recognize its previous -- reconsider its previously issued guidance and provide a list of factors that fiduciaries should use to assess financial strength. We suggest that these factors include many of those detailed in interpretive bulletin 95-1. For example, the level of an insurer's capital and surplus, the quality and diversification of the annuity provider's investment portfolio, the size of the insurers -- of the insurer relative to the proposed contract, the lines of business of the annuity provider, and other indications of an insurer's exposure to liability, credit ratings, the availability of additional protection through state guarantee association, and the extent of the insurers guarantees in the structure of the annuity contract, supporting -- such as using separate accounts.

We'd be pleased to work with the DOL further in identifying the information in terms of where it can be obtained. And in order to avoid any misunderstanding by plan fiduciaries, we ask the department also to clarify that a plan fiduciary will have protection under the safe harbor if the fiduciary gathers that relevant information and prudently evaluates it. We recognize the third recommendation is different from the position we took in response to the proposed regulation, but since the regulation was finalized, our

experience in the feedback we've received from the plan spelled sponsors we interact with indicate fiduciaries really struggle to identify and gain comfort with the specific they should consider. Therefore we think it would be very useful to provide a clear roadmap for fiduciaries by detailing the list of factors they should evaluate.

In closing, just want to congratulate the agencies for recognizing and seeking solutions to addressing the growing need to redefine retirement, through the use of guaranteed lifetime income solutions. I thank you for the opportunity to share our thoughts and look forward to questions.

Robert Doyle:

I guess I have one, at least one question. Ms. Marcks, you've used the phrase redefining retirement, maybe you can tell us what the old definition was and what the --

[laughter].

Christine Marcks:

That's a great question. I -- I think of it -- it's -- it applies to defined contribution plans. And defined contribution plans were originally designed as supplemental savings vehicles because we had a robust defined benefit platform. That is no longer the case, unfortunately and the -- the defined contribution plans were never framed -- they were focused essentially on accumulation and not on what they could provide in terms of a retirement income when somebody retires. Because they are the primary vehicle now for so many Americans to help finance retirement, we believe that the income dimension of what that balance provides and putting options inside a plan that enable participants to get that lifetime income guarantee would essentially redefine retirement for many Americans.

Robert Doyle:

Am I correct in assuming -- this is for either of you or both of you -- that you don't necessarily share the, I guess, pessimistic view of some of our prior witnesses about the value of education in terms of changing the participant decision making process?

Christine Marcks:

You know, I think education is certainly an important part of the whole picture. I'm very supportive of financial

literacy programs. You know, at young ages, we do see people coming into plans, you know, who are in their twenties, thirties, forties and just, you know, have not - - don't have that base of information, so they don't know how to make decisions. The -- actually the default features that were part of the pension protection act have been very helpful in terms of putting some of those folks on a path that they might not be on if they had to make the decision and take the action themselves. So I think education is an important dimension here, but I think there's more to it than that.

Jason Bortz:

Yeah, I mean, in some ways the pessimism is rooted in recent participant behavior and lowered annuitization rates, but there are lots of explanations for why annuity purchase rates have been low recently. I mean, we are in an incredibly low interest rate environment, which obviously has an impact on the annuity amounts you get. We also have a historically thin market place where we haven't had a ton of people buying it, and there's been some adverse selection for that reason. We think as that grows and becomes more robust, it could become much more attractive, so I think we're much less pessimistic and we think education could have an enormous effect to getting people over this hump of, I guess this is the example was before, parting with your \$100,000 and getting the lifetime income stream in lieu.

Robert Doyle:

You think that's a governmental responsibility or should it be left to those in the market place?

Christine Marcks:

I think it's a partnership. I really think it's a partnership. You know, we find different situations depending upon, you know, the type of industry the employer is in, so the needs may vary from plan to plan. There's a foundation there that I think is -- would be very helpful. I mean, I think what we've seen is a concern, for example, as we try and as we talk to planned sponsors about educating their participants on the use of this balance for income purposes, we do run into these situations where employers are concerned about whether they are stepping over the line with regard to advise. So I think the clarification of, you know, incorporating this into an education program is very important.

Robert Doyle:
Thank you.

Rhonda Elming:
Okay. I have a question for Jason with respect to the in-plan accumulation annuities and what you see as the biggest obstacles to being able to provide that under the current regulatory environment.

Jason Bortz:
Yeah, I mean, I think there are a variety of different issues that have arisen. You all have spent a fair amount of time today talking about the fiduciary barrier, and we certainly think that the department of labor can take a variety of steps to, you know, strike the right balance between making sure there's fiduciary oversight over annuities selection, but also not creating an impediment to the offering of annuities. We see sort of a need for guidance on a variety of issues where it's fitting the existing rules into the different qualification requirements. I think I alluded to the qualified joint and survivor annuity rules, which were written in 1998 in essentially the same form and really not designed for these in-plan accumulation annuities. And we'd love to see, you know, a workable solution that still preserves the important public policy underlying those spelled spousal consent rules. So those are some examples.

Rhonda Elming:
Do you have any suggestions on that latter point?

Jason Bortz:
Yeah, I think the main issue is if you treat an investment in an accumulation vehicle as an election of a life annuity that triggers the full-blown spousal consent requirements, you create a number of, sort of, oddities that really don't make sense. For example, the spouse loses the right to be the 100 percent beneficiary and suddenly becomes the 50 percent beneficiary. And more fundamentally, it's at a time at which you cannot get spelled spousal consent because the trigger, the investment in the accumulation annuity, is far before the annuity starting date when you could get spelled spousal consent. And so we think a really basic step forward would be to say, "Hey, a mere investment in an accumulation vehicle does not in itself trigger the spelled spousal consent rules."

J. Mark Iwry:

Jason, further to that question that Rhonda was asking, in your written comments, you went into this in some detail and I understood you to be saying that the -- the trigger for spousal consent that the committee was recommending would be something like irrevocable election? Are we understanding that correctly?

Jason Bortz:

Yeah, I think you are -- that it's really the decision to take a payment in a life annuity and if the payment is going to be taken in a life annuity then it needs to be in the form of a qualified joint-survivor annuity. But if you're talking about a 35 year old, for example, who's investing in an accumulation annuity whether it's something with a living benefit feature or an in-plan accumulation annuity, it's just too soon to believe that that's really an election of a life annuity, so we'd like to see it deferred until it's really made. And that's a time when someone can actually consent, and you don't have these transition issues on the death benefit side. Mark, I'm thrilled you read the letter.

[laughter].

J. Mark Iwry:

I think this is around page 28 of 37.

[laughter].

Jason Bortz:

I thought you might like the table of contents.

[laughter].

Male Speaker:

I was just curious. We're talking obviously within a plan environment here, but have you seen adoption rates outside of the plan environment take up I respect to annuities, maybe in an IRA context, just, what do you say to the market place.

Jason Bortz:

Well, Chris, you may be better.

Christine Marcks:

Well, we have a very robust take-up rate in our variable annuity business where living benefits are actually elected, roughly 85 percent of the time. So, it is a -- not a traditional structure and I think that goes to -- against some of the behavioral dimension that we've seen as we've looked at options here. I mean, nobody would disagree that a single, straight life annuity is, from a benefits stand point, you know, you know, the best you can get. But some of the issues with the irrevocability and -- and control over assets -- there's a fundamental tension there I'll say that where people don't want to give that up, and so these lifetime benefit structures enable that flexibility and control such that people are not afraid to -- to elect them because they do have some ability to make -- to change their mind.

Male Speaker:
Thanks.

Robert Doyle:
Okay. Thank you very much. I appreciate your testimony.

Christine Marcks:
Thank you.

Robert Doyle:
If you have an order, we defer to you. But if not --

Rebecca Davis:
Is it me, okay? Alright, well thank you.

[laughter]

Panel Four

Rebecca Davis:

Thank you for giving me the opportunity to speak today. My name is Rebecca Davis. I am legislative counsel to the Pension Rights Center and coordinator to the center's pensions -- Women's Pension Project. The Pension Rights Center is the nation's only consumer organization dedicated solely to protecting and promoting the retirement security of American workers and their spelled spouses. The center has long been an advocate for retirement plans that provide lifetime streams of payment such as defined benefit plans and money purchase pension plans. That is because we believe a lifetime stream of income in retirement is vital to ensure that retirees do not exhaust their savings. The fact that participants in most 401k plans take their benefits in the form of a lump sum increases the risk that older Americans, especially unmarried women will find themselves in poverty in retirement. I wanted to thank the departments of labor and treasury for initiating a dialogue on how lifetime income options can be brought to 401ks and similar individual account plans.

In my testimony today, I will address questions posed on the hearing notice regarding participant concerns that impact their choices of benefit options, the disclosure of account balances as monthly income streams, and the fiduciary safe harbor for fiduciary selecting annuity providers. I want to begin by emphasizing a number of points made in the written statement that we submitted in respelled response to the RFI. In our statement we recognized that participants have many concerns when declining to annuitize their retirement savings. Because of these concerns, we would support a requirement that all defined contribution plans offer basic lifetime income option as an optional form of benefit distribution from the plan. A basic offering would be a simple annuity base, transparent and subject to the joint and survivor rules applicable to defined benefit plans. There should also be an option for partial annuitization to give participants greater flexibility and also to calm the nerves of those who balk at putting all their nest egg in one basket. Additionally, the mere existence of the benefit option within the plan carries with it an endorsement effect that could encourage some wavering participants to opt for an annuity.

Under current 401k plan structure, participants may withdraw all or part of their savings -- excuse me -- and purchase an annuity on the private market. Alternatively, a small number of individual account plans through service providers, offer participants annuity options. Private annuities are problematic, primarily because of their high cost and the negligible monthly benefits that small account balances can purchase. For these reasons, an annuity option within a 401k for participants with low balances would not be a realistic choice for most low and moderate-income participants. Yet these are the individuals most in need of lifetime income in retirement. Therefore, we suggest that serious consideration be given to the concept of establishing a government sponsored program, ideally administered by the PBGC where participants with low account balances could purchase low cost annuities.

Some of the RFI comments express concerns about limitations on death benefits and withdrawal options, particularly in the form of a required spelled spousal consent before the plan could pay benefits in certain forms. Under current law, the qualified joint and survivor annuity protections are triggered in a defined contribution plan once the participant selects an annuity option. A participant wishing to take an annuity in a form other than a 50 percent joint and survivor benefit must obtain a notarized spousal consent before receiving distributions. These protections are vital to protect the spouse's share of the marital property, but unfortunately because the protections are only triggered after the participant elects an annuity option, they're meaningless in most cases.

A participant wishing to take single life annuity without garnering his wife's consent can simply elect to take his benefit in the form of a lump sum and purchase an annuity on the private market. The only way that spouses will be truly protected in 401k type defined contribution plans will be to require spousal consent before any withdrawal from the account other than a joint and survivor annuity option. The burden of obtaining such consent is borne by plan participants and measures similar to those for defined benefit plans could be put in place to address extraordinary circumstances, for example, where a spouse could not be located. Legislation, of course, is necessary to fully protect spouses, by requiring spousal consent for any withdrawal of funds in any form other than a QJSA. We have for many years strongly supported and advocated for

such legislation, and I would note that the federal Thrift Savings Plan, as mentioned already, currently does require spousal consent for all non-QJSA withdrawals from TSP accounts.

The concerns expressed by some individual comments regarding limitations on death benefits demonstrates that as retirement plans shift from defined benefit to defined contribution plans, there's also a decisive shift in how people view their retirement savings accounts. Many of the individual comments to the RFI stated that one of their motivating factors in saving in a 401k is to provide a nest egg for their children rather than supporting workers and their spelled spouses in retirement which, of course, is the justification for providing the preferential tax treatment for retirement plans. Given that the median 401k balance for private sector workers -- this is age 55 to 64 and this statistic comes from 2006, before the recession -- was \$40,000, it is clear that participant interest in bequeathing assets is a concern of a privileged few who are able to maximize non-retirement savings in their 401k retirement savings accounts. Significantly, in my personal work providing direct legal services to individuals and their attorneys with pension matters, only rarely have I been contacted by a child about their potential entitlement to a survivor benefit from a defined benefit plan. We've been contacted for -- by children interested in their parents' defined contribution plans, but people tend to understand that a defined benefit plan is for the worker and his spouse.

We support a disclosure regime that would provide participants their account balances, both in the form of a monthly lifetime benefit and as a lump sum. To that end, we support the disclosure proposed by the lifetime income disclosure act -- this is Senate Bill 2832, it's sponsored by Senators Bingaman, Isakson, and Kohl -- which would require 401k plans to inform participants of the estimated monthly retirement income they could purchase based on their existing 401k account balance. The bill would afford plan participants personalized information about the purchasing power of their retirement savings. This would give plan participants important information about how much income they can expect in retirement.

In addition to the disclosure of account balances in the form of monthly lifetime payments, annuity providers should

be required to inform participants of the participants' state of residence guarantee fund limits on insurance contracts. State spelled sponsored guarantee funds have maximum guarantees similar to the PBGC that vary from state to state. However, the protected amount varies by state from as low as \$100,000 in Florida to \$500,000 in New York. One of the specific questions mentioned in the hearing announcement asked what mortality table should be used in providing the annuity projections. Current law requires that any lifetime income product offered through an employer sponsored retirement plan must calculate the benefit using gender neutral mortality tables. This requirement provides critical protection to women and should be retained for any lifetime income product offered directly or indirectly by a 401k type individual account plan.

I want to add one further comment on the importance of educating plan participants. The individual comments in response to the RFI overwhelmingly expressed a lack of trust in service providers, employers, planned sponsors and the government as an administrator of lifetime income benefits. We believe that their fears are best addressed by assuring that any implementation of a required annuity option in 401k type plans be accompanied by a large public education campaign. The comments demonstrate a lack of understanding in the value of a lifetime stream of income. In particular, my eye caught a brief comment submitted by an individual who stated that he is married yet chose with his wife a lump sum, because an annuity would have taken away, as he said, a percentage of the benefit from his wife if he died. This was a, you know, 50 percent survivor benefit. This man is the very demographic a public education campaign must reach, a worker who wants to provide a survivor benefit for his spouse, but believes an annuity diminishes rather than bolsters the likelihood that their savings will last for both his and his wife's lives. If this individual understood that an annuity would have enhanced his wife's retirement security, he and his wife may have well opted for the lifetime option.

The current labor regulations provide a safe harbor for plan fiduciaries in selecting annuity providers. The safe harbor essentially provides that if fiduciaries follow current fiduciary duties, they will be absolved of any wrong doing in the selection of an annuity provider. Many of the comments on the RFI requested that this regulation

be clarified to provide an easier method for fiduciaries to meet the safe harbor. We do not have a problem with a modified safe harbor if it requires that plan fiduciaries select among top rated providers with high claims paying abilities that are located in states with strong regulatory agencies and if the products offered do not include investment features. However, we would oppose any proposal that merely diminishes fiduciary duties with respect to the selection of any plan service providers without insuring that the selection will, in the best -- be in the best interest of plan participants. Any lessening of the current requirements threatens the established purpose of ERISA, which is of course to protect plan participants. Thank you for giving me the opportunity to speak, and I am happy to answer questions.

Amy Matsui:

Good morning. My name is Amy Matsui, and I'm senior counsel at the National Women's Law Center. The center is a non-partisan, non-profit, public policy organization located in Washington, D.C. I work in the center's family economic security program area, which focuses on economic issues important to women and their families, including retirement security. The center commends the Departments of Labor and Treasury for making expanded access to lifetime income payments from pension plans a regulatory priority. We appreciate the opportunity to submit comments in conjunction with a number of other organizations committed to women's retirement security, and we're grateful for the opportunity to testify at today's hearing.

Research indicates that retirement savings are likely to be inadequate for many Americans and particularly for women. While there's a substantial gender gap in all sources of retirement income, the disparity between women's and men's DC or account accumulations is especially pronounced. The gender gap in retirement savings is attributable to women's work patterns. Women in general earn less than men; they're more likely to work part time where they're unlikely to have pension coverage at all; and they're more likely to take time out of the work force at some point during their careers. As a result the median female worker, near retirement, with a defined contribution plan or IRA, held less than half of the assets held by her male counterpart in 2004. Unfortunately, women need more and not fewer retirement savings than men because they're likely -- they're more likely to live longer and spend more

years living alone. The National Women's Law Center thus supports requiring defined contribution plans to offer lifetime income options. With intensive education efforts and overtime, we're confident that participants will become more familiar with lifetime income options and can be expected to elect such options with higher frequency.

The departments requested testimony on a number of specific topics. My testimony will cover two of those topics, specific participants' concerns and alternative designs of in-plan and distribution lifetime income options. With regard to the first topic, I'll cover three participants' concerns as they pertain to women: cost of lifetime income options, access to assets, and amount of assets in DC plans.

Lifetime income options offered through DC plans are likely to be less expensive for women than annuities available from insurance companies. First, annuities offered through insurance companies are priced using gender distinct mortality tables, which can result in women receiving lower monthly benefits than men for the same investment in an annuity contract. In contrast DC plans are required to offer annuities that are calculated without regard to gender as required by Title 7 of the Civil Rights Act of 1964. Second, lifetime income options offered through DC plans are likely to be lower priced than annuities offered to individuals on the open market because of institutional pricing. In addition, it would be expected that the price of annuities would drop further as increasing numbers of participants selected annuities.

Several commentators observed in their RFI comments that the gender neutral pricing under DC plans would discourage male participants from selecting annuities. However, general neutral pricing is required in DC plans under current law, and I am not aware of any evidence indicating whether gender distinct pricing is a reason that impacts male DC plan participants' decision making, much less causes them to not select annuities. Moreover, it is possible that the difference between gender preferential and general natural pricing would be mitigated as a result of institutional pricing. But in any event, the departments should not seek to change long-standing anti-discrimination protections on such a speculative basis.

The second concern I'd like to discuss is access to assets. Commentators have also noted that individuals may be reluctant to purchase annuities because they want to have enough liquid assets to deal with unplanned expenses. Low and moderate income individuals, in particular, may be especially concerned that their entire account balance would be locked into a lifetime income product. The center therefore recommended in its joint comments that participants should be given the option of receiving some portion of their account balance as lifetime income, so long as the amount to be annuitized met a minimum threshold amount. The amount of that minimum threshold was obviously a critical question for the departments to resolve.

In our experience, even relatively small amounts of dependable lifetime income can be significant for low and moderate income workers. The minimum account policies in DB and federal Thrift Savings Plans are instructive. DB plans must annuitize benefits with a present value in excess of \$5,000 and the Federal TSP must do so for account balances above 3,500. With regard to these systems, therefore, policy makers have determined that those amounts which would result in only very small monthly payments are significant enough to warrant annuitization. We therefore reiterate our recommendation from our joint RFI comments and encourage the departments to conduct a joint study to determine an appropriate minimum account balance for purchase of an annuity with the needs and likely account balances of low and moderate income workers in mind.

The third participant concern I'd like to discuss is the level of assets in a DC plan account. Some participants may be concerned that the assets they've been able to accumulate in one employer's DC plan are insufficient to make a lifetime income payout option worth their while. Although participants can contribute up to 16,500 per year under current law, few workers, especially low and moderate-income workers, do so. Only six percent of women making a contribution to a 401k type plan made the maximum contribution in 2005, compared to nearly 12 percent of men making contributions. However, participants may have other retirement savings accumulated with other employers since the average worker has multiple jobs during his or her career. Thus as a worker nears retirement, he or she may have retirement savings in one or more DC plans and in one or more IRAs.

Many women have saved enough throughout their careers to provide for a modest but not insignificant supplement to Social Security. In 2004, the median 401k and or IRA account balance for women aged 55 to 64 was \$34,000. O

ne annuity calculator estimated that a 64-year-old female in the District of Columbia who purchased a fixed immediate single life annuity with \$34,000 from an insurance company could expect monthly annuity payments of \$193. Although it would be impossible to live off this amount alone, it would provide an important boost to Social Security payments which average about \$1,000 per month. Unfortunately, unless an individual could aggregate his or her accumulated retirement savings in the 401k account that offered a lifetime income payout, he or she would be unable to maximize his or her lifetime income payments. Under current law, a DC plan may but is not required to accept rollovers from other qualified retirement accounts. We therefore recommended in our joint comments that plan administrators be required to accept rollovers from other qualified plan accounts and conduit type IRAs.

The second topic of my testimony is alternative designs of lifetime income options. In 1984, Congress passed the retirement equity act or REA. Pursuant to the REA, the default form of benefit for married participants in defined benefit plans is a qualified joint-survivor annuity or QJSA. A QJSA provides an annuity for the joint life of the employee and his or her spelled spouse and a survivor annuity of at least 50 percent of the spelled spouse after the employee's death. The spelled spouse can waive the QJSA following certain procedures established by statute. Congress's intent in enacting the RA -- REA, was in part to "Provide for greater equity under private pension plans for workers and their spouses and dependents, by taking into account changes in work patterns, the status of marriages and economic partnership, and the substantial contribution to that partnership of spouses who work both in and outside the home."

The need for that equity has not diminished 36 years later. As DB plans have been increasingly supplanted by recite -- retirement saving plans like 401ks, but the protections of the REA do not apply if married DC plan participants do not elect their -- to receive their benefits in the form of a life annuity. A married participant can make the decision to take a lump sum or roll the account balance into an IRA

when he or she changes jobs or retires without any input from his or her spelled spouse. Spousal pension protections are vital to women who are more likely than men to rely on their spouse's retirement benefits.

One recent study indicated that almost 24 percent of women age 60 and over received DB pension income from their spouse's former employer compared to about seven percent of men in 2006. Survivor benefits from DB pensions more specifically have a significant impact on women's retirement security. After congress passed the REA, the number of married men who provided a joint-survivor annuity for their spelled spouses increased 23 percent. In 2006, women age 60 and over received a median survivor benefit of \$7, 850 per year, a not insignificant amount. Moreover, the data suggests that DB pension survivor benefits help lower income older women avoid poverty. A disproportionate number of women receive DB pension -- receiving DB pension survivor benefits fell within the second lowest income quintile rather than the lowest income quintile, suggesting that DB pension survivor benefits made the difference. In addition, women receiving DB pension survivor benefits were less likely to fall below the federal poverty level. The importance of spousal pension benefits, and in particular, the survivor benefits provided through a QJSA therefore should not be minimized.

Some groups have recommended amending the QJSA rules as applied to some or all lifetime income options that might be offered through DC plans, asserting that this would encourage more employers to offer lifetime income options. For example, commentators asserted that QJSA protection should be eliminated all together or should not apply to distributions from hybrid products that essentially represent payments from account balances. Similarly, commentators recommended that employers be offered to -- permitted to offer lifetime income options through an RIA platform administered by a third party to which QJSA protections would not apply under current law. We're sympathetic to employers' concerns regarding administrative burdens and costs, but some of these proposals would effectively eliminate spousal protections which are so important to women's retirement security. If plans are required to offer lifetime income options to further the goal of expanding access to lifetime income in part to counter the retirement insecurity posed too many workers by DC plans that goal would be undermined by eliminating

spousal protections required under current law. In addition, this loophole in retirement security particularly affects women and low-income women more so.

We're also concerned about proposals that seek to expand the use of electronic technologies to administer QJSA requirements beyond what's permitted under current regulations. ERISA requires that spouses waive spousal pension benefits in writing in the presence of a notary public or plan administrator. This is intended to reduce the possibility of fraud given the importance of the benefit being waived. Treasury recently considered the extent to which electronic technologies should be employed in the transmission of spousal consent. The Treasury regulations provided that electronic procedures may be used to effectuate spousal consent only if "Reasonably designed to preclude any person other than the appropriate individual from making the election," and in particular, if the procedure's "provide the same safeguards for participant elections as are provided through the physical presence requirement." Accordingly the Treasury regulations allow spelled spouses to provide consent with an electronic signature in the presence of a notary public or plan administrator, but they explicitly reject the use of pin numbers or telephonic technologies. We with some of our partners asserted that this is in part because a pin number is particularly susceptible to being used by a spouse inside the house with a motivation to do so.

With rapid advances in technology, we anticipate the development of procedures that would provide the same security as the physical presence requirement, but with regard to pin numbers, under current technologies, we agree with Treasury's recent conclusions that those methods would pose a serious threat to spousal rights. In sum, spousal protections in retirement savings are extremely important for women and reducing those protections in the hope of encouraging employers to offer greater access to lifetime income presents a significant risk that policy makers should not take. In conclusion, I appreciate the opportunity to testify at today's hearing, and I look forward to respond to any questions that may relate to areas covered in my testimony. Thank you.

Cindy Hounsell:

Good morning. Thank you for letting me testify today. I'm Cindy Hounsell, the president of WISR, a non-profit organization with 15 years experience providing women with the education and tools to help them avoid poverty in retirement and raising awareness amount policy makers and the public on the unique retirement risks that women face. WISR also operates the National Education and Resource Center on Women and Retirement Planning under a cooperative agreement with the Administration on Aging. The center is a gateway of information created with strategic public-private coalitions to provide hard to reach women with financial tools and actionable information. The center's goal is to help low and moderate-income women make the best decisions they can with what they have. The center has directly reached 10s of thousands of women through our workshops and our partner workshops. We've reached millions with our publications and website. Our approach is to bring financial planning back to the basics. Our strength is to provide women with core financial knowledge that encourages them to make financial retirement planning a priority in their lives.

In May, AARP, ASPR, and WISR sponsored a lifetime income summit. The summit provided a unique opportunity to learn how the financial and insurance market innovations are addressing gaps in lifetime income security. I think it was a great conference and a great opportunity, and I know many people in the room today were there. Key findings released from the summit can be found at -- on the website at Lifetimeincomesummit.org. We're very hopeful that the agencies' hearing will help to step up on to the adoption of policies that were discussed to help increase participant education and to fill in lifetime income gaps.

The risks women face. The term lifetime takes on a whole new meaning for retiring women. Millions of women will live a third of their lifetimes after they reach age 60. Thirty years is a long time to make their savings last, putting women at high risk for poverty in their old age. Many of the longevity risks women confront simply come from factors operating throughout their lives that affect their ability to save and build assets and Amy's talked to us about some of those statistics already, so I won't belabor that point. And she also mentioned that in theory women should save more money than men because they live longer, and they'll need more money to support themselves. As they age, they're also likely to have more incidences of chronic

illness and will need additional funds to pay for higher expenses. At the same time women are not saving anywhere near the amounts that are needed for a longer retirement. The most pressing threat women face in retirement is outliving their assets. Running out of money in retirement is too large of a risk to self-insure. But that's what millions of retirees attempt to do in an era of lump-sum distributions from defined contribution plans. Women need the best information and tools to help them determine how much income they will need, where the money will come from and how to make it last. They need access to safe, affordable lifetime income products.

Our statement today will respond to the first three issues included in the Federal Register's hearings notice. The first, certain specific participant concerns affecting the choice of lifetime income relative to other options. There's ample research and WISR has sufficient anecdotal evidence showing that participants take the lump sum option because they lack information. They lack financial capability and do not have an understanding of longevity risks or why they might want to pole these risks and receive income for as long as they live. We hear that the language used to guide participants often has the opposite effect and acts as a deterrent for people deciding whether to annuitize. We hear story after story of people of people who take the large sum and put it in a cash account, terrified that they'll lose it. A typical story is a couple receiving \$250,000 dollars. The wife explains they didn't trust the information they were receiving, so they just took the money, and then the vultures descended and would not leave them alone. She said that the vultures included her grown children as well as several financial planners who wanted to help them.

Aside from his issue of individual trust is a lack of trust toward financial institutions, especially following the economic crisis. Despite state guarantee fund for immediate annuities, people fear that the company that sells them the product will go bankrupt and be unable to pay the promised benefit. And I think they have good reason to believe that since we all know about the big, large company that went from too big to fail to -- there still there, anyway, in whatever form their in.

[laughter].

I'm a loss for words. But it's difficult for people and how else do they know, and we need transparency, and we need guidance from the department I believe so that people have a way to compare, not that most of the people I ever talk to have a way to compare. They don't even know. They just know, I'm either going to take all the money or I'm not going take all the money. So I think talking more about partial annuitization is also something that we really need to begin to push.

Lifetime income products are not without their limitations. For example, they can fix -- they cannot fix inadequate savings. They typically do not adjust for inflation, eroding the annuitants purchasing power over time. Although providers are increasingly coming up with features to address issues like this, they often come at the cost of higher expenses and lower income pay out. We're hopeful that the products will continue to improve with the advent [spelled phonetically] of the boomer retirement. Also, the decision to accept a lifetime annuity is typically irreversible. Studies show that people fear this aspect on the chance that they may die before they receive the cost of the annuity back. We often tell women that the problem for them is that if they live for a long time, their heirs wouldn't get anything back anyway, and that their heirs might end up having to support them. And then there's also the issue of control. We've seen story after story about people taking a lump sum and leaving on the table an annuity with the cost of living adjustment just so they have control over their money. We believe that government policy should help people with their decision making. WISR has worked with the actuarial foundation for nearly a decade to help people understand why they need to understand annuities. We'd like to work with the agencies to provide the best information for people so that they can more easily make these life-defining decisions.

Information to help participants make choices, I'll address that. Until recently, policy discussions have focused largely on asset accumulation. Accumulation is, of course, a critical ingredient to retirement income security, but we need to help people see the big picture. How can they make use of what they've earned and saved to make their money last as long as they do? Education we see as a key missing link. Combined with Social Security, immediate annuities represent a meaningful channel through which millions of women can live out their years in comfort and

dignity. Yet, despite their availability few retirees opt for lifetime products. We've talked about that ad nauseum. Less than 20 percent of retirees age 65 and over receive retirement income in the form of an annuity. Women are in the difficult position of having to make these decisions with little guidance while being unable to afford to make even a small mistake. Many women are unaware of even the basic challenges that they're facing. Education should help them understand the risks of retiring too early, of outliving their assets, and the impact of living alone.

Women can receive actionable information through employers whose surveys show time and time again are the trusted messengers. We need to help employers educate people and make it easier for them. I think there needs to be a place where medium and small employers can send their employees to get the trusted information they need. I'm very sympathetic to the issues that employers have to deal with. I happen to be a former union representative for a great company that's now out of business. So, I've seen both sides and I know the difficulties that you face when you're providing a benefit and yet you have to worry that everything you say may create another problem.

One quick story I'll tell. We were working with a large company on a research project with a consumer booklet that accompanied the research. Great booklet, if I may say so myself. The company representatives were so pleased. They kept telling me how popular it was and how really great it was, copies flying off the shelves, several reprints within a year. Someone suggested that it was such a great booklet, let's put in Spanish, and somehow it got to the Spanish compliance person, who added about five pages of regulatory -- I call this blah, blah and I don't mean any disrespect to the regulators -- but to the average person -- we all know the average person would think of it as blah, blah, and after that it became a fifteen page booklet with disclaimers on every page. I mean, I was almost afraid to read it for what would happen to me. The end of the story is that after that the English version, you know, conformed to the compliance, the booklets were no longer flying off the shelves, and it became something that we didn't want to use either.

We know that people can learn if they're given the right information, and I believe that the -- even the decumulation stage, otherwise known as the rest of your

life is what I call it can -- can help people realize how different needs and circumstances will involve different ways of making money last. We think there needs to be a roadmap or guideline for employers on how to educate their employees about these important choices on how to take distributions. WISR works through organizations that have trusted links to a constituent base with millions of women. We have talked and spoken to thousands of women, and we believe that it can be done. But the decumulation stage is much trickier than the earlier stage of accumulating assets. Every aspect of a worker's financial life needs to be considered before such an important decision is made. What expenses will need to be covered by their retirement income? Will the house be paid for or will an annuity need to cover those expenses too? We need to reframe the discussion so that the pursuit of lifetime income, not the prospect of a onetime lump sum check is the goal of retirement planning. Educational efforts need to build better awareness about the tradeoffs of retirement income options. New online tools made retirement planning more accessible to more people. Educational efforts should draw attention to all of these new -- the new technology and useful tools.

At the lifetime summit, the hit of the day, was the tool that was highlighted by Robert Reynolds, president and CEO of Putnam, and I only say that because, really, everybody seemed to be excited, but maybe it was a whole day of annuities and we all had to find something to be excited about.

[laughter].

But he provided a demonstration of their lifetime income analysis tool, and the tool was designed to provide participants with an assessment of how well they're doing in accumulating income, and it just seemed like it did everything. It showed you how much you had, if you changed it, it would -- like going to one of the retirement planning calculators, but it was all part of your particular 401k and had your information so I -- I presume that there are probably, you know, hundreds or thousands of these other great tools, but this was the one that we all happened to see and think was terrific. And I think things like this will make a lot of the conversation having today even moot in a couple of years because people will just have better tools.

Finally, on the disclosure of account balances, it sort of follows in to what I was just saying because the lifetime income analysis tool also did that. Defined contributions are the primary retirement plan. One step is to show the assets on statements in the form of lifetime income. We agree with all of that -- as I said, I think in a few years it may become a moot point. It could become a moot point before we get another bill introduced next year. But I think that the agencies should encourage employers to educate workers about lifetime income and also the -- those four letters that Chris Marcks. What are those letters?

Christine Marcks:
Oh, GMWB.

Cindy Hounsell:
There you go. GMW --

[laughter].

Oh another of -- I'll never get that one straight.

[laughter].

Anyway, we recommend that the agencies work with industry leaders and other interested players and develop a set of best practices on financial awareness of retirement income options, all of them. The recent lifetime income summit showed there was a lot of agreement. People need quality information and the American public needs it soon, and we look forward to working with you, and I won't read you my conclusions. So, thank you.

Robert Doyle:
Thank you. Questions? Comments? Observations?

J. Mark Iwry:
I'll -- I'll start. Cindy, in the WISR written submission, you discussed the importance of spousal consent and preserving the spousal rights and also discussed the potential advantages of an in-plan annuity option, including to women because of the unisex pricing requirement. In the previous panels, we've heard about proposals to facilitate the in-plan annuity option by clarifying how the spousal consent rules would apply, including a suggestion that spousal consent should not

attach at the time participant makes an investment decision in a deferred accumulating annuity but rather at the time the participant actually commits themselves to taking the benefit as an annuity. So, it's the -- it's the irrevocable decision to take an annuity rather than to invest in something that may become an income pay-out. Do you have any comments on that whole issue of how the spousal consent rules might appropriately and whether they should be interpreted in the context of these in-plan annuities or what the general approach ought to be, and I would ask the same question of Amy and Rebecca. If all three of you would offer your thoughts, that would be appreciated.

Cindy Hounsell:

I would -- I would acquiesce to Amy and Rebecca who are --

Amy Matsui:

Is it fine if I start?

Rebecca Davis:

Yeah, yeah.

Amy Matsui:

I'll go ahead and start. I think our understanding of when the spousal consent rules apply is based on the private letter ruling that was issued in 2009 and understanding that that has limited precedential effect, but just the idea that when an election to receive the income -- to receive the distributions is made that's the point at which the consent rules apply. That being said, I think that a concern is that there are a lot of different products proliferating, and I am not familiar with the particulars of each one of those, and I think that there could be a concern in this context where broad decisions are being made about what's going to constitute a valid lifetime income that's going to qualify as a valid choice under a DC plan. What are the policies underlying those?

Do the participant concerns about flexibility and ability to withdraw -- how are those balanced out with the interest in maintaining lifetime income, because that's the future of an annuity, it lasts your entire life; it's guaranteed. There are obviously issues around whether or not they are going to be adjusted for inflation which can affect the value of those payments later on in life, but those are certainly two major competing considerations when trying to

determine what's an appropriate product to be called a lifetime income product that would meet the goals of this policy and so to that end, you know, I think that I'd be reluctant to base that -- to make recommendation based on a ruling that applies to one kind of product. It's a very broad decision that's going need to take all those factors into consideration. But certainly, you know, under the current rules, the -- the election to receive a form of benefit is what triggers the QJSA protections.

Rebecca Davis:

I don't know if I have anything further to add on that. I agree with Amy.

Male Speaker:

I have two questions. Thanks for your testimony. It was very compelling. First Ms. Hounsell, you talked about work you did with the -- what was it-- the actuarial foundation?

Cindy Hounsell:

[assent]

Male Speaker:

Have you, with respect to that work, have you found any educational approach that works, that changes behavior, that increases adoption rates, anything in that work that you would want to share?

Cindy Hounsell:

Well, I mean, I think the problem is, and I keep saying that the book I should've written was no one knows anything and I think that's pretty obvious by anytime you look at any one of these financial crisis and all the people that go ahead and do the things that you would think they should know better than to take those steps. So I think just letting people understand how annuities work; most people just don't have any idea. And people wouldn't even begin to understand that you could just do a portion of your money. A lot of people don't know, I mean, really, we need to get back to basics. And I -- it doesn't matter the educational level, WISR does a program here behind the capital with -- and it's actually part of an ICI grant, and I'm always amazed if I go in, and I say, "Okay" -- and these are people who don't have jobs; they're getting their GED, and I say, "How many people here know about a 401k?" Practically every person raises their hand. What do you know about it? "Enron." I mean, you couldn't even

get that probably from the general public so it -- it doesn't matter. You'd be surprised at what people do know, but you'd also be surprised at what they don't know.

And so I think what we found is that giving people the basics and helping them to understand that, you know, this may be something you don't want to do when you retire because I think timing is a big issue. A lot of people, when they're retiring, don't want to do that whole annuity piece. They, first of all, they haven't registered that they're retiring and they're getting older. So maybe five years from then they might want to do it, and that may not be the best answer for everyone but, I'm just saying, I think it's really a very, a very difficult -- it's much more difficult to educate around than it is to tell people to save more. So -- I don't know --

Male Speaker:

And then, secondly, Ms. Davis, you talked about a low and moderate income individuals and the need for a government spelled sponsored program to support the purchase of annuities. Could you just expand on that, any more details that you have with respect to that idea?

Rebecca Davis:

Okay, well I think it's a good time to mention Pension Rights Center, in partnership with several other -- excuse me -- several other organizations, launched an initiative a couple of years ago called retirement USA, and in this initiative, we as a group adopted fourteen principles. And one of these principles -- well, USA stands for Universal, Secure and Adequate. We're looking for a retirement system's that's universal, secure, and adequate for the next generation. Today, we're talking about the current generation of retirees and those approaching retirement.

But one of the principals that we adopted was that we would like a system where there's a lot of trust that can be garnered in the financial institution that is maintaining the -- that's providing the annuities, that people can have a trust in their system to encourage them to go in to annuitize. And particularly in the low and moderate-income employees, where they're saving, you know, small income account balances, we think something like the PGVC, a non-profit institution, you know, we're saying government institution in my statement but to look into the PGVC, a non-profit, a government, something where it's a reliable,

you know, there's no profits being made. It can provide a low-cost annuity option for people with low account balances.

Male Speaker:
Okay. Thanks.

Robert Doyle:
Any other questions? Thank you very much for your testimony. In fact, we'll thank all those who testified this morning for their testimony, and we will temporarily adjourn and reconvene at 1:45.

[lunch]

Panel Five

Robert Doyle:

Welcome back, everyone, and we'll start our afternoon session. And I think with that, we'll turn it over to panel number five.

Elizabeth Heffernan:

Thank you.

Robert Doyle:

We'll let you maybe introduce yourselves.

Elizabeth Heffernan:

Thank you. We'll go in order, as others have. So, I'm Elizabeth Heffernan representing Fidelity Investments. Fidelity Investments is one of the world's largest providers of financial services with assets under administration of 3.3 trillion including 1.5 trillion in assets under -- investment assets under management. Founded in 1946, the firm is a leading provider of defined contribution record-keeping administration as well as other services, including investment management, portfolio guidance, and brokerage to 20 million individuals as well as thousands of institutions and secondary firms, such as broker dealers. Fidelity is also one of the largest providers of income annuities and other insurance products. Our retired customers have purchased over \$7 billion of immediate income annuities as a means to add lifetime income protection to their spend-down strategies.

During my 15-year career with Fidelity, I've worked with plan sponsors and participants in a variety of roles focusing on retirement plan and participants planning for a comfortable retirement. Fidelity has helped millions of Americans transition to the retirement phase of their lives for many years, but there is more to be done. And we need your help through further expansion of the current interpretive bulletin that will allow for increased guidance tailored to the unique and individual needs of workers to not only plan for retirement but to spend for retirement.

First off, though, in Fidelity's opinion, the most pressing retirement challenging -- challenge facing American workers today is quite simply people are still not saving enough. Our research indicates that during a worker's active years,

they need to be contributing at least 10 to 15 percent or more, including their employer contributions, to reach a comfortable retirement. Workers who wait face a significantly higher requirement. Only this type of dedicated savings from an early age can a worker even hope to realize retirement savings adequate to provide income for their retirement years.

Unfortunately, the realization to save often comes too late, far too late to make up for years of little or no saving. No lifetime income or guarantee solution will make up for an inadequate balance. So, we -- our first priority still needs to be focusing on getting people to save for retirement.

Considering today's topic of lifetime income, we need to focus not only on the way in which workers accumulate assets though, we do need to focus on the way they will withdraw assets from defined contribution plans but also from IRAs. Plan sponsors, plan service providers, and IRA providers must offer educational tools for retiring workers focused specifically on the spend-down phase of retirement. Education and guidance in this area should help individuals assess the five key risks of retirement income. Longevity definitely, but also inflation, withdrawal rate risks, market volatility, and health care.

Prior to the issuance of Interpretive Bulletin 96-1, Fidelity and other providers submitted samples of educational tools that would allow participants to see concrete examples of a diversified asset allocation strategy. Accordingly, the bulletin provided safe harbor for modeled portfolios that comprised actual plan investment options for hypothetical participants with similar risk and time horizons. Now, to parallel that existing education that illustrates investment diversification, new tools must provide the user with corresponding asset class or product allocations to provide lifetime income. Ultimately, a user may be shown an illustration with a mix of individual investment options and income-producing options as one possible way to achieve the selected product allocation given the user's stated preferences. Interactive guidance could also give the user the ability to change the illustration and make substitutions.

We believe that the proper legal framework for such guidance is contained in the bulletin although certain aspects are not specifically addressed. For example, an investor who chooses an annuity gains longevity protection and the promise of payment for his or her lifetime no matter the length, but this purchase, however, needs to be examined against the loss of liquidity that will be experienced and the need to consider the availability of other non-annuitized investment options.

Additionally, given the diverse nature of retirement income needs, all of the investor's income sources and assets need to be taken into account. We do not see anything in the current wording of the bulletin that would prohibit the creation of this guidance. However, in light of the increased focus on lifetime income, we would request that the department provide confirmation of the beneficial nature of such educational guidance.

Additionally, a critical component of education and guidance is to create an income mindset for people saving for retirement. Without an understanding of the relationship between retirement savings and potential retirement income, people far too often underestimate the savings needed to fund what might be more than 30 years in retirement. We believe the most effective way to provide this information is through a simplified, generic illustration based on methodology prescribed by the agencies that shows how retirement savings could translate into an income estimate.

For example, the illustration could show the range of monthly income that \$10,000 might generate starting at 65 based on assumed interest and mortality factors. The illustration could be accompanied by the appropriate caveats and disclosures. While an illustration based on a person's actual defined contribution value might be helpful, that person's current defined contribution is unlikely to be their own defined contribution plan or their own -- only retirement savings. The generic illustration would facilitate consistent application of an income estimate to all of someone's retirement savings accounts.

The income illustration would simply be a starting point. Retirement income planning can be complex, given that everyone has different income needs, sources of income, and goals in retirement. Additional guidance tailored to the

individual circumstances including retirement plan assets, non-plan assets, detailed budgeting, and consideration of other income sources in retirement is not needed to provide the more focused guidance to help workers make specific saving and distribution decisions. We have conducted more than one million income planning sessions with our pre-retiree customers and all of those sessions included an analysis for the need for additional guaranteed income, especially to cover essential expenses throughout retirement no matter how long that may be.

On the issue of choice, and as stated in our lifetime income comment letter submitted earlier, Fidelity believes that whatever regulatory framework is designed should provide the availability of all types of solutions and not exclude or favor a specific approach, product, or industry. Rules should continue to encourage the variety and innovation that presently exists in the marketplace, thus providing defined contribution plan sponsors the freedom to choose that most appropriate -- most appropriate for their employees and providing participants, including IRA account holders, a choice.

Products that provide some form of periodic payment stream -- so-called "lifetime income products" -- are available in a wide variety of forms. These include fixed and variable annuities, fixed income funds, systematic withdrawal plans, money market funds, bonds, and dividend paying securities. Fidelity has long been a leader in making these products available and will continue to provide lifetime -- innovative lifetime income solutions to investors as the market demands.

We believe the diverse range of retirement income needs and the tailored solutions that must be developed to meet the individual needs are best handled through out-of-plan solutions for pre-retirees and retirees. The current challenges to in-plan solutions, including plan fiduciary concerns, general costs and on-going price competitiveness, portability, participant behavior, and demand, are not easily remedied. And one-size-fits-all default solutions cannot meet the diverse and individualized needs of retirees. At Fidelity, the average age of a retiree purchasing an immediate income annuity is 67. This suggests that it is only after retirement that people begin to truly assess and understand their various income needs and to construct a financial income plan for their

retirement years. Additionally, their plan needs to be flexible enough to change to adjusting personal circumstances as well as changing market conditions.

I want to thank you for the opportunity to testify today. In summary, we would urge further expansion of the current interpretive bulletin that will allow for the increased guidance tailored to the needs of workers to not only plan for retirement but spend for retirement. Workers should be encouraged to save more from an early age and we urge you to do all you can to emphasize that point.

Finally, we do see the need for better guidelines to help workers adopt an income mindset that allows them to easily translate what they have saved into a reasonable monthly income estimate. Our commitment to our customers is one of life time engagement. We are driven to establish relationships that will help all of our customers achieve lifetime goals, most notably retirement. We look forward to continuing to work with you to assure a comfortable retirement for all working Americans. Thank you.

Edmund Murphy:

Good afternoon. My name is Ed Murphy and I lead the defined contribution workplace savings business for Putnam Investments in Boston. Thank you for inviting us to testify.

I want to begin by applauding regulators and policy-makers in Congress for the continued emphasis we're seeing on vitally important retirement security issues, notably the recently introduced legislation to provide auto IRA coverage for millions more American workers -- which we strongly support -- and this hearing itself, which reflects the very timely focus by DOL and Treasury on lifetime income policy issues.

At Putnam, we believe that providing for future income is the prime rationale for all forms of tax-deferred retirement savings, notably defined contribution plans, which have become the primary source of most American workers' future retirement income. Yet this central goal -- lifetime income, which was a key focus of most defined benefit plans -- has too often been obscured by an emphasis in most defined contribution plans on total account balances, asset allocation, and investment options. These are all important metrics and should be readily available

to workplace savers. But we believe that the primary focus or framing of workplace savings should change to emphasize the true goal workers are aiming for: lifetime income.

Workers should be enabled to see their job-based retirement savings plan through a lens that offers them a clear understanding of their account's potential for generating reliable income for life. They should also be enabled to understand intuitively the actions they can take to increase their retirement income potential and the cost-benefit trade-off of taking such actions. With those ends in mind, Putnam this January introduced a new Lifetime Income Analysis Tool that sponsors of the workplace savings plans we administer can use with their participants.

This online tool provides workplace savers a new and very different experience. It shows them -- as the first information displayed when they log on -- an estimate of their projected monthly retirement income needs expressed in current dollars compared with the potential monthly retirement income they are on track to create in their workplace savings plans based on current balances, their current deferral rates, and asset allocation choices, and their projected retirement date.

This tool thus enables plan participants to get a sense of whether they are on track to maintain their current lifestyle once they stop working -- or will likely fall short. To make this analysis richer, the tool also allows participants to include projected Social Security income in these estimates, factor in other non-plan financial assets -- such as bank CDs, individual retirement accounts, spousal savings -- and calculate how these flows and assets impact their potential income at retirement. Participants can also see clearly how much of their future income will derive from any matching funds their employer may provide -- a feature that makes this often invisible benefit highly visible.

Most importantly, the tool has a bias for action. That is because it has three sliding tabs that enable participants to alter their deferral rates or their projected retirement age or their asset allocation mix and immediately see the impact of that change measured in terms of future income potential. The tool also suggests a projected next step -- a prescriptive recommendation on an action most likely to close any income gap their interaction has disclosed. One

further click of the mouse and participants can immediately change their current deferral rate, their asset allocation, or their projected retirement age.

Through this site's basic design, then, the lens through which participants view their workplace savings has been changed significantly. Putnam's initial experience with this process strongly suggests that the new view does, in fact, influence participants' savings behavior. We are actually seeing a phenomenon that few of us in the retirement services world thought we would ever see: impulse savings.

Preliminary data shows that of participants who visit the Web and use the Lifetime Income Analysis Tool, roughly one-third submit a change in deferral rates immediately. Four out of five participants -- over 80 percent -- choose to lift their savings rates by an average of more than two full percentage points -- from 6.1 percent before their site visit to 8.6 percent; that's a 40 percent increase. This result is a real breakthrough, a degree of change that is rare, almost unheard of, from traditional communication and education efforts. It suggests that if you give participants a clear, easy-to-act-on understanding of the trade-off between higher deferrals today and higher income in retirement, many of them will act immediately.

This data comes from analysis of aggregate behavior by plan participants in July and August of this year amid sluggish economic growth and at a time when some industry surveys showed substantial increases in hardship withdrawals and loans from workplace savings plans. As a veteran of an industry that has struggled for many years to raise deferral rates, I find this initial data on the impact of offering participants a clear, easy-to-act-on income view to be very, very encouraging.

To make an income view an effective motivator, however, it is vital that financial services providers be permitted to calculate estimated future income potential based not just on current account balances, but on contribution rates and potential asset appreciation to some future retirement age. Expressing a participant's progress in terms of their account's immediate lifetime income-generating potential could actually undermine confidence and de-motivate savers. Such an approach -- immediately converting current balances into the lifelong annuity income they could purchase right

now -- could be perversely discouraging for younger employees with smaller balances and would, in fact, vastly understate the future income potential they are on track to achieve at a retirement age.

We believe that participants should have access to full disclosure of the methodologies used in calculating their future income needs, the income potential their savings plan are projected to have at retirement age, and all other elements that go into providing good faith estimates of how they are faring. We do present this information on our website. We also provide clear disclosure language to ensure that participants understand that there is uncertainty associated with these projections and that it is their responsibility to visit their plan at least annually in order to accommodate changes in the market as well as changes in their own financial situation.

In terms of long-term policy impact, my sense is that participants who learn to interpret their workplace savings through the lens of their future income potential will be much more willing as they approach retirement age to consider products and services designed to convert their balances into lifetime income streams. Regulatory and policy action that encourages financial service providers and plan sponsors to emphasize an income view of workplace savings could help speed the adoption of such an approach and begin changing workplace savers' mindset about their goals.

We would also support efforts to offer plan sponsors and advisors a strong legal safe harbor for advocating or adopting plan design elements that emphasize a lifetime income view or for offering participants education and guidance to appropriate lifetime income products and strategies.

Thank you for listening.

Bob Collie:

My name is Bob Collie. I'm here to represent Russell Investments, a Tacoma, Washington-based research, consulting, and asset management firm.

Your premise today that the defined contribution system should be built around the provision of income throughout retirement rather than simply the accumulation of assets is

sound. Current disclosures, however, are a barrier to this objective. They facilitate inattentive and too often unsuccessful behavior from plan participants because they fail to make clear how the progress of the investment portfolio and the choices that the participant makes are connected to the standard of living they can expect in their retirement.

Today, I would like to do three things. First, I will explain how to improve disclosure of account balances, then I will explain the need to standardize those calculations, and finally, I will describe the wider context of the retirement income system of which disclosure is a part.

You can and you should improve disclosure by showing a lifetime income equivalent to the current account balance. Doing so is actually remarkably simple. We should not tell the participant only, "Here is your account balance." We should also tell the participant, "Here is how much income that balance would buy for you today, for an older version of yourself who has reached retirement." That is a simple, meaningful, robust number. You could add further information: how much more income is likely to be available after retirement if you allow for future investment returns in excess of inflation. What if the participant makes further future contributions? All of these future events can be taken into account in supplemental disclosures. What happens if the retirement age is changed? Every added layer supplements that first income number but it requires more assumptions to be made about the future, assumptions that become more subjective with every layer.

All of those supplemental numbers are helpful, but the essential number is what income does the current account balance provide? There are several advantages to making that the basis of disclosure. First of all, it is a very simple calculation. Assumptions are needed only for interest rates and mortality. This aside, actuaries are more than capable of providing mortality tables that can be used for this specific purpose. Prevailing interest rates can be observed in the markets at any point in time.

The second reason that this number is so valuable is that it is the number that is the closest equivalent in terms of income to the account balance on which plans currently report and indeed to the Social Security statements with

which most working age individuals in this country are familiar.

Thirdly, although simple, it is a meaningful disclosure. By nature of how it's calculated, it's automatically expressed in today's dollars. It assumes survival until retirement and general levels of mortality thereafter. Those are appropriate assumptions.

And finally, it is objective. It is objective because the lifetime income equivalent to given sum of money is something that can be derived relatively easily from the market for annuities. This might be packaged, as suggested in the announcement of these hearings, as a standard program produced by the agencies designed to broadly mimic the market's annuity pricing basis or indeed it may even be possible to simply issue each month standard tables of appropriate annuity factors.

Now, none of this means anybody has to buy an annuity, but the option exists, and that provides a market-based objective measure of what the lifetime income equivalent to a given sum of money is and that's what we should be seeking to report. I would incidentally suggest that you disclose an annual modern monthly figure. That's partly because it will go some way towards solving this perception problem that we have where \$100,000 doesn't look like a lot when it's turned into \$550 a month. It's also because people don't think of their income in terms of monthly amounts and other contexts. They think of them in terms of annual amounts.

My second point is that reporting should be standardized. It shouldn't depend on who calculates the number. It would cause all kinds of confusion if different service providers give different answers to identical people with identical account balances. This happens today and the differences are big. My colleague, Dr. Bill Madden, recently compared the results and recommendations for a hypothetical plan participant whom we called Sharon based on five tools currently available to participants. The conclusions were sharply divergent. One indicated that Sharon would need to save only a little more to be on track to meet her retirement goals. Another found that she would have to save an additional 44% of her salary each year to do so.

That is ridiculous. These extreme variations in results highlight the dangers of a non-standardized approach. The only way to prevent it is to standardize the calculations. Obviously, standardized numbers do not foretell the future. There is uncertainty in every element that needs to be standardized, but at least standardized numbers would have only basic and unavoidable uncertainty and would handle it in a consistent and transparent fashion. There will inevitably be variability from year to year in the income levels that are disclosed. Annuity rates vary just as all other markets do. So even with a standardized basis, that basis itself will vary from year to year and the income disclosures will change each year.

However, participants are already accustomed to seeing their account values vary, but that information is none the less universally accepted as an objective and fair assessment of the situation at that point in time. It's the same with income disclosures. They too will vary; that's life. It would do more harm than good to withhold the best available information just because we don't like what it shows.

I should emphasize that a standardized basis should be neutral on questions of different investment strategies, neutral on whether to purchase an annuity or a different retirement income product or to self-fund, neutral on whether to invest actively or passively, neutral on stable value target date -- all of those questions. There's no intent here to endorse any particular approach to building retirement program. Similarly, a standardized disclosure calculation should not restrict service providers from developing planning tools, such as the one Ed has described. Those are useful tools and should be encouraged. But the simple changes that I've suggested would represent an important step in the realignment of the defined contribution system toward retirement income focus.

To wrap up my remarks, I would like to put the question of disclosure into the context of the wider system. [unintelligible] analysis set out in a recent book "The Retirement Plan Solution," which I coauthored with Don Ezra and Matt Smith. In this book, we describe three types of defined contribution retirement system which reflect three different attitudes towards what the plan is aiming to achieve.

The first is the bank savings model, which is how the very early 401(k) plans were built. These were designed to provide a tax-efficient savings vehicle and to invest it mainly with the goal of capital security. The second model, which has largely replaced the first, is what we call the fun supermarket model in which investment choice and growth of assets become the primary goals. But it's only in the third of our three models, which we call the retirement income model, which explicitly considers the objective of a post-retirement income stream that lasts for a lifetime. There is no good reason that today's system should adopt the fun supermarket model rather than the retirement income model. It does so largely because the defined contribution system in the U.S. has been shaped by happenstance as much as by design.

Disclosure alone will not turn an imperfect system into a perfect system or move us instantly from a fun supermarket approach to a retirement income approach but disclosure is an essential component. It's a necessary step towards such goals as better savings rates, better take up where appropriate of investment choices, such as annuities or other retirement income products. Disclosure of progress in terms of retirement income simple and standardized along the lines I've suggested would be a force towards a better system because, as it's frequently been said, what gets measured, gets managed.

I respectfully submit these comments for your consideration and would be happy to answer any further questions that you may have.

Paul Stevens:

I'm Paul Stevens, president and CEO of the Investment Company Institute, the national association of mutual funds, exchange traded funds, and other registered investment companies. I'm very pleased to be here to be able to share our views.

My remarks will focus on three issues that the agencies would like to explore further: first, specific concerns that may deter workers from selecting annuities rather than other distribution options; second, what information would help participants make choices in managing and spending down retirement benefits; and third, whether and how to disclose account balances as monthly income streams.

There are two ways to approach the question of why workers are not electing annuities over other options available to them. The first is to look at what priorities and goals, other than meeting longevity risk, a worker or a retiree might reasonably entertain when deciding how to manage his or her retirement assets. The second is to look at current retirement resources to determine the extent to which Americans are already annuitized. We were pleased that the agency's hearing notice recognizes that meeting longevity risk is not retirees' only objective. Our research shows that savers and retirees also want access to their assets in case of a health crisis or other emergency. Many desire to leave assets to surviving spouses or children or have other priorities. ICI research shows that retirees demonstrate a strong desire to retain control over their retirement wealth so they can deal with these and other important life issues.

Fortunately, the market for retirement income products has evolved to address all these legitimate objectives, varying though they may be. A worker approaching retirement can select a product or mix of products along a continuum. One solely concerned with longevity and with securing a stream of income that preserves purchasing power until death can choose an inflation-indexed immediate life annuity. To meet other priorities, workers can add other features, such as death benefits or guaranteed pay-out periods. These can be bundled with an insurance product or replicated through other strategies; for example, by combining a basic annuity with investment accounts ear marked for emergencies or other needs. At the other end of the continuum are self-managed periodic withdrawals.

What's important to note is that each step along this continuum involves trade-offs among numerous factors? These include how much control a retiree surrenders over his or her account balance, the amount of immediate income a retiree receives, the retiree's desire for guarantees, the ability to access assets for emergency needs, inflation, credit, or other investment risks one wishes to assume, as well as the longevity risks. Public policy should recognize that each retiree has his or her own mix of priorities and that each can employ different methods calculated to meet those reasonable objectives.

The agencies also, in our judgment, should recognize that Americans already are highly annuitized through Social Security, defined benefit pension income, and home ownership. While DB pension coverage has declined, millions of current workers can still expect to retire with DB pension income, especially those who spend some or all of their careers in the public sector.

Social Security is, of course, an inflation-indexed immediate life annuity and is central to America's retirement security. In 2006, non-working individuals age 65 or older received 51 percent of their income from Social Security. For half of this group -- the lowest incomes -- that figure was 85 percent. Research from the Michigan Retirement Research Center shows that among households in their mid-50s in 2006, annuitized assets, including the present value of Social Security benefits, accounted for 93 percent of wealth in the poorest quintile. Even in the wealthiest quintile, 52 percent of wealth was annuitized. These data suggest -- and there's a graph in my written submission to the panel -- these data suggest that if Americans want more annuity income the demand is much more likely to come from higher income households.

So the strong desire Americans express to control retirement assets to meet competing concerns may reflect the recognition that the bulk of their wealth is already annuitized. And that, in turn, suggests that the primary concern of public policy should be ensuring that workers and retirees have access to clear and comprehensive information about their options and the trade-offs involved.

What information will prove most helpful to participants in managing their retirement benefits? We believe that good education depends on both the content and the delivery of the information. In our judgment, good content would meet four specific goals. First, it would get Americans to identify the range of income and assets that they have to help fund retirement; not just DC and DB benefits and certainly not what happens to be in their 401(k) account at the time that they are entering retirement, but also all of the retirement assets they have plus Social Security, housing, other assets and income, or assets provided by a spouse. Second, it would get Americans to identify their goals and anticipated needs in retirement and to consider the impact of unanticipated medical or economic

developments. Third, it would inform Americans on the many alternative ways to structure their affairs to provide regular income, cope with emergencies, and meet other objectives. Fourth, it would provide general information on products and strategies to meet these goals and concerns, including clear information on the objectives, the risks, the trade-offs, and the costs.

Now, ICI has long advocated and approved disclosure for all retirement products. Costs and trade-offs must be clear for all options and choices and particularly so for complex financial products like annuities. Participants are most likely to make sound decisions when they are provided all the facts. Any other approach would fly in the face of our long-standing policies for financial products.

Now, delivery of information is just as important as the content. Decades of research has shown us at ICI that disclosure is effective and useful when it is clear and concise, it makes use of graphics, it provides layers of information, and it makes effective use of technology. Now, these principals can serve plan sponsors and participants very well. They're incorporated in the summary prospectuses that many mutual funds are now employing. This approach turns the either/or choice of providing more or less disclosure into a both/and system. Investors receive both a short summary document tailored to provide the most important and useful information and the many additional layers of information are made available to them through the internet. Workers would benefit from such an approach because plan record-keepers tell us that participants tend to make contact with their plans through the internet.

One specific informational issue is whether workers should receive statements that translate account balances into estimated monthly income for retirement. We believe this is useful information and many ICI members -- some of whom on our panel today -- are working with the plans they serve to provide such calculations. We do not, however, support mandating this disclosure or codifying a single approach to calculating or providing the information. Instead, the agencies should let the market continue to evolve, to discover what information participants find most useful, and how best to present it.

If instead policy makers do choose to mandate such disclosures, they must be clear about what objective this disclosure serves. We believe the proper objectives are to help Americans understand what monthly benefits might -- they might expect if they're current elections stay in place and to help them analyze whether their retirement savings are on track or not. My written statement contains several specific recommendations to make such disclosure clear and useful based on techniques that are already proven in Social Security and other investment statements.

Thank you for the chance to appear today. I assure you that the institute and all of our members intend to be full partners with government employers and others as we work to enhance retirement security for all Americans. I'll be pleased to take any questions you might have.

Robert Doyle:
Thank you very much.

Male Speaker:
Well, I'll start if no one else will. Can you hear me okay? Okay. I'd like to ask a few questions about the usefulness of providing someone's account balance in the form of a stream of income. After listening to all of you, I'm not quite sure where Fidelity comes in on it because you talked about a generic example, a generic illustration, but the -- the other three: All of you seemed to support that idea to one extent or another. The ICI concluded by saying, "But don't mandate specific assumptions. Allow the industry to fill in the gaps." But on the other hand, Mr. Collie stressed the need for uniformity and standardization. And so I'd like for you to explain how on the one hand, standardization is absolutely needed but on the other hand, flexibility to choose and vary standards is a good idea.

Edmund Murphy:
Could -- can I take a shot at it? It seems to me there are two issues here. One is whether you take the account at present or whether you look at the account out -- in out years. The other is how you then depict what the amount is that could be received in current income. And there you have an election between looking at it as a drawdown from an investment account where the assumptions are fairly clear or doing it as an annuity where I would say, for most people, the assumptions are going to be rather more opaque.

I was thinking as I prepared for the hearing today about my son, just gone -- entered into law school and served -- he was 18 months in a law firm here in town and he has a very, very small 401(k) balance. If he receives a statement that talks about what an immediate life annuity with the balance in his 401(k) is, he's going to think, "That's inconsequential. Why should I keep this account? I have expenses. I have an automobile I need to pay for." And you will incentivize a young worker with a long investment horizon that a 25-year-old has to think of that balance in improper terms. That's why I don't think there's one size that's going to fit everybody here and the agencies ought to forbear, at least for now, and let the market evolve in the way it's responding as clearly it is to these kinds of concerns.

Male Speaker:

Well, that may be how your son reacts, but others may kick themselves in the butt and say, "I need to save more."

Edmund Murphy:

Well, I hope he will over time when he can.

[laughter]

Male Speaker:

The -- but, so -- but you raise another issue and that is the extent to which any expression or depiction of a person's account should focus on that which is accrued at the time of the statement versus projections. And I understood the Putnam online tool to project. Is that correct?

Edmund Murphy:

Yeah, think about it in the context of a -- graphically, think about it in the context of a paycheck. So, what we do is we take the current balance that you have in your account and we show the stream of income that that will generate at retirement. We then take the current contribution rate and we look at what that generates over time in the form of a monthly payment. And then we provide the ability to model different scenarios, and the three key inputs are deferral rates, age you're going to retire, and investment mix.

So, you know, I agree with what Paul is saying that to just show current income based on the current balance, the income that's generated off the current balance doesn't really tell the whole picture.

Male Speaker:

So, you would support projection of --

Edmund Murphy:

Yes.

Male Speaker:

-- what your current account balance buys you at retirement.

Edmund Murphy:

Yes. We look at -- we take a look at the asset classes, fixed income, equity. We look at 70 years of historical returns. And then we run, you know, millions and millions of Monte Carlo simulations.

Male Speaker:

And do you think the regulators should encourage that or mandate that sort of requirement?

Edmund Murphy:

Well, what I would say is this industry has struggled for years to change behavior. There are companies that spend over \$100 million a year in participant education and advice and we have not been able to move the needle on deferral rates until recently. So, you know, our experience is, you know, limited to the time we announced -- introduced this tool back in February, so we're still learning as we go. But the fact of the matter is we're seeing material change in participant behavior.

Male Speaker:

You said a 30 percent change in deferral rates?

Edmund Murphy

The average participant increased their deferral rate from 6.1 percent to 8.6 and of the folks that made a deferral change in July and August, 80 percent of them increased their deferral.

Male Speaker:

It'd be interesting to know if you have the data that cut that by account balance size to see if the -- Paul's son -- the reaction was, you know, consistent with that 30 percent uptick.

Edmund Murphy:

Yeah. We -- we would have that information. We, have all the salary data so --

Male Speaker:

Okay.

Edmund Murphy:

-- we'd have that.

Male Speaker:

Now, Mr. Collie indicated that -- his idea was a baseline, right? Two assumptions. Nothing particularly dramatic here -- mortality and interest rates -- but then if you begin to project, then things get to be complicated.

Bob Collie:

It gets to be -- and as I said, I would encourage exactly the type of projections that you're describing. As you're probably aware, the Australian Securities and Investment Commission have actually put out guidelines that would go around similar [unintelligible] down there.

I would argue though that that's quite a separate supplemental issue than the one of baseline disclosure. We have the opportunity to take current account balances. The idea of projecting future account balances is nice; I mean, it's a good planning tool, but that's not disclosure. We're used to current account balances and that should be the basis for the basic lifetime income.

Again, if it's a small number, well, it is a small number. That, in the early days of a savings plan, the reality is there's not a great deal of accumulated income yet. It's step one in a path. I don't think you make system better by disguising that reality. I mean, there are two realities that underpin the provision of retirement income. One, it is expensive. If you want to retire at age 60 or 65, you may be saving for 35 or 40 years trying to pay for a retirement that's almost as long. That costs a lot of money. We can't by sleight of hand make that go away. And

we can't make go away the fact that investment returns won't serve them.

Male Speaker:

I assume you'd also have to disclose, though, and I didn't hear any mention of this, to the individual that -- in connection to this that you surrender your account balance. I think that that would be a very, very important additional disclosure. That's fine; you can make those calculations but you also have to tell the individual your account balance now goes to zero. You get that income but what you're buying for it is what you have in your account.

[speaking simultaneously]

Bob Collie:

-- you know people can handle that.

Male Speaker:

I think to Paul's point -- the younger saver -- does it make sense or I'd be interested in the group's view to the significance of maybe limiting a mandate to an older part of the workforce or whether we start to undermine this kind of disclosure?

Elizabeth Heffernan:

Yeah, I think that's why we advocated for a sort of starting with a generic illustration so people just get to look at a sort of a common number and start translating to an income mindset, but -- I think most providers, including us, also have those more detailed tools that you want to drive people to to then do a much more in-depth individualized planning process so that they can start taking into account what am I actually doing and what will changes to my behavior do to that illustration? If I save more, how much does that impact my income or change asset allocation or change my retirement years?

I think the challenge you have with delaying, I think to Bob's point, is that it comes a shock to people the first time they see that translation, and so if you start creating at least some connection to the basic mathematics of the estimate then people don't get so surprised when they see 100,000 is "X" amount annually or "X" amount monthly. That's what we're trying to drive at is you've got to start connecting people to that translation.

Male Speaker:

I have a question for Mr. Murphy. I was impressed and shocked with the increase in deferral rates that you've seen and, you know, the previous panels have suggested that the -- to really see a significant change in behavior would almost require a very significant investment of educational resources; the government could or could not be a part of that. Are there other things that were done in addition to the advisor that helped to create the outcome that you've seen? Were there other variables at play in creating that kind of increase in the deferral rates?

Edmund Murphy:

Well, I think the challenge in terms of driving the adoption rates higher and seeing more individuals take action is making it simple and intuitive and easy for them. And, you know, this is -- in my view, this is sort of the first inning in a nine-inning game and, you know, what we would want to do at Putnam is we would want to drive more activity to the Web because it's graphical and it's a way to engage them.

I think that, you know, one of the things that's been a key driving factor is that we illustrate what the trade-off is. So, if, in fact, you are going to increase your deferral rate, we show what the impact is that -- in pretax dollars and then we show what that translates to in income in retirement. So you can make an informed decision as a participant. You can say, "Look, if I defer an additional \$150 a month. So, I'm -- I move my deferral rate from 4 percent to 5 percent, that's going to translate into \$475 in retirement per month and I increase my match an extra \$20. Do I want to make that change?" I hit the button, two clicks, it goes to payroll; it's done. If the next day, I decide that I've got to write a check for my son's student loan, you could actually back your deferral rate up again.

So, I think it's just it's -- you know, it's making it simple, it's making intuitive. It's showing what the trade-off is and that's how you change behavior. It's obviously much more easier to do that on the Web where you can engage them than it is over the telephone. So, I think in terms of us driving adoption rates higher, we need to think more creatively on how we can drive more traffic to the Web.

Male Speaker:

And just in terms of demographics, you think the change is even across different demographic groups in terms of salary, in terms of age, you're seeing parallel increases across the board?

Edmund Murphy:

Well, I think, you know, if you think about most higher-income workers, many of them are at the max deferral rate or near it, so most of the activity that we're seeing is more in the mid-level compt and lower-level compt employees but I can you the specific salary data to support it.

Male Speaker:

When I think about this problem, I'm reminded of some of the learnings we get from behavioral economics, which is that basic presentation is what's going to -- what people are going to think. "Oh, that's what the government thinks I should -- or whoever's sending me this document -- that's how I should take the money out." So if, in fact, it says, "This is how you calculate it base on a 4 percent withdrawal rate," they're going to assume, "Oh, 4 percent withdrawal rate's the way to go." If it says this is based on a retirement age 65, well, that must be the right way to do it.

And one other particular framing of this question is if it assumes a life annuity versus a joint survivor annuity, there is going to be, "Well, that's the recommended point." Of course you can vary it; sure, the Web has the power to have different models. Have you thought in terms of what is the message that you want to provide if you were having a single framing point in terms of how this projected accumulation is going to be distributed as lifetime income.

Bob Collie:

You want to be as neutral as possible, which, again, is why I said let's use a single objective market point and, I mean, as you say, if someone has a low account balance which translates into a low income if they buy an annuity, one obvious conclusion your son may reach is, "Well, I'm not being an annuity then." So you can interpret the income conclusion however you wish. Correct decision making does require correct information. To the extent you can frame it as neutrally as possible, you should.

On the question of joint survivor or individual, simplicity would unfortunately push you towards probably having to do the individual because marital status can change. You can be married today but not at the point of retirement and vice versa. You don't know the age necessarily of the spouse and so on. So, you would want to be very careful to make clear -- or maybe this is the place for generic example: The typical joint survivor annuity will be whatever the number is -- 80 percent of the amount of a 401 -- you would want to think carefully about the framing but you shouldn't stop that from making any disclosure at all.

Male Speaker:

Well, to Harlan's point, have you thought about the commencement date? That would seem to me to -- it could be normal retirement age, 65, you could tie it to --

Bob Collie:

Tie it to Social Security, again, there's an age at which Social Security works around so that's the obvious default. It's not necessarily right in every case but that would be the simplest.

J. Mark Iwry:

Well, as the ICI's testimony written statement pointed out, of course some people might be advantaged by, depending on their circumstances, delaying Social Security commencement --

Bob Collie:

Yes.

J. Mark Iwry:

-- to some degree or as far as they can depending on, again, the circumstances. So, isn't there -- how would you help us if the departments were to, for example, decide that it would be helpful to issue some guidance giving some comfort to plan sponsors that choose to provide an income equivalent to the account balance. And in that case, of course, it would be -- since it would be up to the sponsor whether to do this at all or not, it would likewise be up to the sponsor whether to have an age cut off and provide those equivalences for everyone over age "X" so that the 20-somethings might not be included or everyone who is within a certain number of years of some retirement age.

But is there any help you can provide to mediate the trade-offs between the merits of standardization that you've been talking about and the need to minimize complexity and length that's obviously part of the presentation. I gather that part of the beauty of what Putnam is doing is that by putting it on the Web, you're allowing people to play with the assumptions --

Edmund Murphy:
Right.

J. Mark Iwry:
-- and therefore, they're not necessarily confronted with an elaborate set of numerous examples in order to ring the changes and all the plausible variations and potentially deter someone from reading the thing entirely. Is that the way to go or are you thinking that the best way to go is some combination of encouraging particular scenarios or examples -- illustrative examples -- plus perhaps if the plan sponsor wishes to do that and a Web-based tool such as yours do that as well?

Bob Collie:
I mean, I think you need both and I would encourage the tools with flexibility, but I think on the basic disclosure, the employer is actually in an easier position if it's not even optional, if you say, "Here's the factor to use to turn a sum into an income equivalent, an annual income equivalent. Just go do it." Then everybody knows where they stand, so everybody automatically has a safe harbor because they're all doing the same thing. And on top of that, you can then build these planning tools. But they meet two different goals.

J. Mark Iwry:
May -- may I just follow that question? So, if you were to assume that the whole exercise were optional with the plan sponsor as it is today, where some plan sponsors choose to provide income equivalents in their 401(k)s or other defined contribution plans, and most don't, then if we were to -- if the government were to provide some kind of safe harbor or illustrative examples that would give employers a degree of comfort if they chose to be among those who offer this income equivalent information, are you suggesting that even there there'd be a particular path, a particular set of assumptions that is stated to be safe as opposed to a range or a band?

Bob Collie:

I would prefer the standardization especially because otherwise you do have an incentive. As a provider, you want your projections to look better than everybody else's. You're going to push the top of the upper limits of whatever ranges is provided and so on. The -- it's much easier. Everybody's playing from the same rulebook and you know [inaudible] --

Paul Stevens:

You know, Mark, I think what happens then is you have frozen the system in amber. You will get that disclosure and only that disclosure and it may or may not serve everybody's best interest but it will have a degree of certainty about it. I think frankly -- and what Putman's come to the table with today is an indication of the very deep thought that many providers have given to this question. They've come at it from different ways and not to feather their nests or make their performance look good but because there are honest differences of opinion about how you depict this complex information.

If the department came up with some examples of what seemed to be reasonable approaches and said, "These are things we would encourage employers to do and if they do this, it would be fine with us," but not mandate it, not freeze it in place, I think that could very well be constructive but it's a complex exercise as I think you all appreciate.

Edmund Murphy:

Yeah, yeah, I would agree. You know, frankly, we're not in the business of giving advice directly to participants, so all the appropriate disclosures are there and we encourage them to work with their advisor and they can work directly with the advisor and model these scenarios together. So I don't think we want to do anything that stunts creativity and ingenuity because this is a major issue that we're facing and in some respects I think the industry has lost its innovative edge and we need to get back at it.

Robert Doyle:

Go ahead.

Male Speaker:

I'll try to be quick. Just one clarifying question and then one sub-issue that I don't think we've dove into yet.

The clarifying question: Mr. Murphy, the numbers that you gave of the impact of the tool, did you say those were numbers for people who had chosen to visit and use the tool?

Edmund Murphy:
Correct.

Male Speaker:
And so what -- maybe you said this already, but what proportion did choose to use and visit the tool?

Edmund Murphy:
It's about roughly 30 percent of the people who went to the site actually modeled the -- used the sliders to model the various [unintelligible] --

Male Speaker:
But what I'm asking is how many of the participants who had access to this site went to it?

Edmund Murphy:
It's single digits.

Male Speaker:
And that's in a two-month period you said?

Edmund Murphy:
Yes.

Male Speaker:
Okay.

Edmund Murphy:
Yeah.

Male Speaker:
Thank you.

Edmund Murphy:
Yeah.

Male Speaker:
The sub-issue that I want to look at just very quickly is projecting forward with respect to asset allocation. So if I understood correctly, the tool has a slider that speaks to asset allocation?

Edmund Murphy:
Correct.

Male Speaker:
And so I'm presuming, you know, that if you slide toward higher risk, higher return asset allocation that the center of your expectation for income goes up?

Edmund Murphy:
To a certain point.

Male Speaker:
To a certain point.

Edmund Murphy:
Right.

Male Speaker:
But you also mentioned Monte Carlo simulations, which suggest to me that somewhere you're also looking at the width of the possible outcome. So if the amount might go up, at least to a point, the width would also get wider, and now I find myself thinking do participants understand that and how is the tool able to get that across to people? And alongside that, you talked about how the tool actually caused people to change their contribution. Did it change them to cause their asset allocation and how?

Edmund Murphy:
That's a good question in terms of the asset allocation. We're still monitoring that. We don't have a lot of good data on changes in asset allocation. The focus of this recent analysis that we did was on deferral rates.

Male Speaker:
Okay.

Edmund Murphy:
In -- I think, as you know, that the key driver in retirement savings is to save more; it's not asset allocation per say, so we've got more work to do on that. Again, keep in mind, we just really launched this in February so we're learning as we're going here.

In terms of how risk gets represented here. So, you have those three variables: retirement age, deferral rate, and

asset allocation. And we basically modeled every single scenario so when you move those sliders, its immediate real-time response. If you're a -- if you're a 60-year-old male and you're retirement age is 65 and you're showing a material gap and that gap is, you know, 75 percent of your current income as your lifetime, you know, retirement savings balance and you are let's say at 6,000 a month and you need to be at 5,200, it shows that you're at 4,400 so you have a gap of 800 a month. Invariably, if you're maxed out on your deferrals, you're going to try and move the asset allocation, right, to go into equities and increase the waiting in equities. What happens is the tool will -- it'll start to decline, the gap will decline, and then as you increase the equity exposure, all of a sudden, it bumps and the gap starts to increase again because you hit that point of diminishing returns if you will where as a 60-year-old retiring in five years, you're overweight in inequities and as such, you're increasing the risk. So we've built the mortality into -- the mortality and retirement age into the asset allocation.

Male Speaker:

Okay. The last dangle on this, and in terms of -- so, for Mr. Collie, in terms of standardization, if we were to say something about these types of forward projections, would standardization mean that we would need to say something about the distribution of returns to different kinds of investments or would it be better just to have a single rate of return no matter was asset allocation had been chosen by the participant?

Bob Collie:

Depending on the purpose. I think for the disclosures that we're talking about here, a single return would be best because to try to use this disclosure to answer the question of asset allocation I think is asking too much of what we're talking about here. I think it's appropriate within the planning tools, but I think it is too much to ask within the basic disclosure.

Female Speaker:

I guess I was just going to make a comment that it just seems from listening to all of you that maybe a combination of these approaches might be the best way to educate because for a younger person, having any kind of example showing the time value of money and what happens if you put money away now and you let it accrue for a number of

years is valuable but then, as you get older, having a tool that you can manipulate to see where you are -- so maybe we should be looking at a combination of these methods.

Robert Doyle:
Thank you.

Panel Six

Robert Doyle:
Welcome.

Tracey Flaherty
Oh, thank you. Ready for us to start?

Robert Doyle:
I think we are.

Tracey Flaherty:
Great. I'm going to go ahead and start for our group. Ladies and gentlemen, on behalf of Natixis Global Asset Management, I would like to thank the Departments of Labor and Treasury for this important opportunity to comment on issues relating to lifetime income for retirement plans. I am Tracey Flaherty, senior vice president, Natixis Global Asset Management, one of the 15 largest asset managers in the world with assets totaling \$650 billion as of June 30.

As it relates to retirement, our affiliated asset management companies manage pension assets, sub-advise insurance portfolios, implement managed account programs, and through advisors, we offer a variety of products for individuals and retirement plans. Let me begin by commending you for sponsoring the forum for gathering information and encourage dialogue on a significant issue of vital importance and major national concern to millions of individuals and families. This hearing is an important step in the recognition by policy makers to create common ground in a fragmented industry, streamline the regulatory process, offer improved transparency and education, and provide real solutions for retirement plan participants.

Retirement income planning is complex and for many plan participants, successful planning requires a carefully balanced mixture of vehicles to create a portfolio that meets the needs and timeline of a participant while minimizing complexity. Considerations often must include longevity risk, inflation adjustments, and withdrawal options. But no matter the plans or strategies employed, we believe there are four prime universal concerns that should be regarded as action items for immediate consideration. First, offer, choice, and flexibility. Most individuals planning for retirement today factor Social Security, employer savings, and personal savings

among their retirement vehicles. Where investments are concerned, no single investment product or style should dominate the search for retirement income options. Annuities, mutual funds, alternative investments and other financial planning sources should all be considered.

We can no longer base retirement planning simply on the age of an individual. Age alone does not tell you enough about the individual or their family. I know 48-year-olds with college-age children, some who are empty nesters, and some like myself, who have a toddler in diapers. All three represent different life stages that require different retirement savings strategies.

Americans also have diverse visions for their future. For example, according to a national survey conducted this past July, 52 percent of American pre-retirees say they envision that they and their spouses will work full-time as long as health permits, yet 21 percent of those surveyed plan to work part-time and another 27 percent look forward to stopping work altogether. The diversity of these responses indicates why maximum choice of retirement strategies is needed to give participants the flexibility to choose the right retirement solution or solutions for their needs.

As an asset manager that offers a wide variety of mutual funds, we believe that in addition to annuities, mutual funds offer many different types of people an effective vehicle for covering accumulated wealth into retirement income. Mutual funds are broadly used, well-liked by Americans, and are owned by over 50 million households. In addition, the flexible nature of these investments makes them particularly well-suited to generating lifetime income. The variety of mutual fund offerings across hundreds of different security types, investment styles, and income sources make them particularly well-suited for building a robust, diversified income lifetime income portfolio.

While annuities may not be as widely held as mutual funds, they are a smart choice for investors as well. Research shows annuities are popular among those who hold them with about one in five people saying they plan to add more and an additional 27 percent of Americans who do not own annuities say that they are interested in these investment products.

Our second concern is insuring optimal portability. Portability of retirement assets or the ability to move retirement savings from one qualified plan to another has become a significant concern. Workers are changing jobs more than ever; the average years for a person to hold the same job is 4.1 years, resulting in an average of 7 to 10 jobs in a lifetime. As a result, the average employee could participate in several retirement plans during his or her career. Additionally, workers want the option to take their retirement money with them when they change jobs. A recent study revealed that over 70 percent of retirement plan participants are not comfortable leaving money in a retirement plan where they no longer work. Care should be given to prevent locking a participant into one product with one firm. Workers may be more willing to use retirement plans if guaranteed that their assets can move easily with them from employer to employer while retaining the benefits unique to qualified retirement plans.

Our third concern is enhancing education. Easy-to-access information and proven, effective education initiatives are a must in the ongoing effort to shift the focus of retirement participants from accumulation to the best way to generate a reliable income throughout their retirement. Simply put, retirement savers of all ages must understand that the goal of retirement planning is to build an adequate retirement income. The current fragile economy and the recent financial crisis have generated a growing demand for retirement plan transparency and real-time information. A recent study shows that 60 percent of participants want more personalized and effective communication, such as websites, proactive emails and on-demand videos; 80 percent of participants are interested in information about how to improve their retirement savings plans. I think you heard, consistent with what you heard from Putnam, from Ed Murphy just a few minutes ago.

But just providing information is not enough. Many plan participants will be unlikely to research, analyze, and educate themselves about their plans. The features begun with the pension protection act, such as auto-enrollment and its intended safe harbor provisions should continue to be encouraged. Automatically showing participants a retirement income calculation as part of their benefits statement would help the education process as well. And finally, a set of simple, retirement education best practices could also be designed to provide easy to

understand and useful information needed by most plan participants.

Our fourth area of concern is keeping it simple and streamlining regulation. The best product with the best education is not going to change retirement savings behavior if the rules and regulations are not made easier to implement by both employers and employees. Policy-makers considering ways to help individuals with retirement planning should consider simplifying the complex and often inflexible rules that govern retirement programs. We know that participants consider individual retirement accounts, employer-sponsored retirement plans, and Social Security as part of their retirement savings. Each has their own complex set of rules and makes using the combination together or separately ever more difficult. Confusing regulations and fear of costly mistakes can deter employees from participating in retirement plans and can discourage sponsors from offering retirement programs. Focusing attention on simplifying retirement plan regulation is one of the best results that this hearing can have.

In summary, we urge the Department of Labor and the Department of Treasury to take timely action on the four prime areas of concern that we have outlined here today. Addressing these four major retirement plan issues, finding effective methods to offer choice and flexibility, providing optimal portability, enhancing education and streamlining regulation are critically important steps in helping Americans save more for retirement. Tackling these concerns and developing workable, effective solutions will provide vital answers as the search continues for ways to increase the financial security in retirement.

I want to thank you again for the opportunity to provide our thinking on lifetime income solutions. We appreciate your consideration of the information presented at this hearing and we welcome the opportunity to respond to any additional questions.

Brooke?

Brooke Worden:

Good afternoon. My name is Brooke Worden and I am a vice president in the financial services industry practice at Weber Shandwick, which is a global public relations agency. I have 17 years of experience in the financial services

industry and have spent the past decade working with retirement service plan providers. As part of providing my clients with strategic counsel, I have developed industry thought leadership programs that explore retirement savings barriers, specifically as they relate to lifetime retirement income options and employer-sponsored plans, generational differences between baby boomers and younger workers, and women who have historically have encountered more significant barriers to achieving retirement security. Additionally, I provided strategic counsel to the business roundtable's Pension Coalition as it worked shape the landmark Pension Protection Act, or PPA, which was signed into law in 2006. And more recently, I served as the public relations lead for the 2010 Census Integrated Communications Campaign.

My testimony today reflects my personal interest and commitment to the retirement security issue as well as the shared commitment of my firm, Weber Shandwick. Weber Sandwick applauds the U.S. Department of Labor and the Department of Treasury for convening this critically important dialogue on one of the most important and defining issues of our time, and I thank you for the opportunity to appear before you today.

My assessment of the current state of the retirement services industry landscape is shaped in part on my work on the PPA and, as described in my recent opinion piece which appeared on Plansponsor.com in early August. Four years ago when the PPA was finalized, the feeling was that while it was not perfect, the act was a step in the right direction in helping more Americans to achieve retirement security. Over the next two years between 2006 and 2008, there were bumps in the road. Not surprisingly, there were some who said that the PPA did not go far enough, and an even more common criticism was that it didn't move fast enough. Some plan sponsors were slow to adopt its provisions and participants continued to fall behind in their retirement savings. Meanwhile, all of us working in the retirement services industry continued to watch and wait for the title wave of baby boomers to retire in droves, or so we thought. And then came the financial crisis of 2008. The world changed, and the concept of retirement in America changed in a way that the PPA never could have foreseen.

Even prior to the onset of the financial crisis in 2008, the retirement services industry was under enormous pressure due to an aging population, the shift away from traditional defined benefit plans or pensions to defined contribution plans, and the overall decline in personal savings to name a few. The financial crisis served to amplify these pressures and by the end of 2008, baby boomers in DB plans indicating they were postponing retirement while total assets in DC plans had declined by over a trillion dollars and target-date funds had lost nearly 30 percent of their value on average. The result was a crisis of confidence and the PPA went from seeming historic to prehistoric because things had changed so significantly.

Looking back to 2006 as a communications professional, the retirement communications of the PPA era have taken on an almost museum like quality. The images of the content from that time often show carefree baby boomers strolling on the beach or smiling as they imagine retirements within their grasp. And today the lucky boomers are the ones who are still working. National Public Radio recently reported that the unemployment rate among boomers is 7.7 percent, the highest rate nor record for workers age 55 and older since World War II. We could not have foreseen a seismic economic shift of this magnitude four summers ago. The other thing that's striking about communications that sought to shape the PPA is that social media was virtually absent and this would be unimaginable today.

In addition to exploring new channels such as social media for exploring the distribution of retirement education and information, it is my belief that a new mindset is needed as well, one that makes the shift from retirement savings to retirement income. Historically, with respect to workplace retirement, virtually all of the attention has been placed on the accumulation side of retirement planning. The result has been that many retire with few strategies or resources to help them decumulate their savings in retirement in a manner that provides a steady stream of income for life. It is my belief that future educational efforts should develop more attention to the decumulation phase and both plan sponsors and plan participants have important roles to play in their success.

I would like to say a few words, if I might, about the role of both the plan sponsor and the plan participant.

Employers are a key channel for delivering retirement income education to their employees, and they are uniquely positioned to encourage workers to save for retirement and through retirement. However, today's plan sponsors wear many hats and face increasing pressures to do more with less, to answer more participant questions, and to balance their role within the regulatory environment. Plan sponsors need adequate support in order to educate their employees about retirement. Many plan sponsors have been slow to adopt retirement income solutions because they are still considered new and untested. And it is my belief that greater education and support for them is likely to spelled speed adoption. In the new economic reality, plan sponsors must be better equipped and educated to be part of the solution to the challenge of achieving retirement security for all.

In terms of the role of the plan participant, today's workforce is increasingly diverse, and new educational initiatives are needed to address our rapidly changing demographics. The first look at the 2010 census results in just a few months is likely to further emphasize this point for us all. Reaching a diverse population of workers is a challenge to consider very carefully and often, and really it is not enough to merely reach these workers and inform them. In order to truly succeed, an educational effort must persuade them to take action on behalf of their own retirement security. Communicating in the new reality, post 2008, means plan sponsors need to be surrounded with retirement income education from multiple sources. Their plan sponsors the government, social media, earned media coverage, trusted organizations, industry influencers, and participant materials. In other communications campaigns my firm has undertaken for federal government agencies and in the private sector this surround sound model of communications has produced the desired outcomes, desired behavior changes, and delivered measurable results.

I'd like to conclude my testimony with some spelled specific recommendations for any new educational effort considered or undertaken by the government. My firm's experience shows that any successful public education campaign should be grounded in research. As an immediate next step, a thorough review of existing financial literacy and financial education programs delivered at present by the federal government should be undertaken. This review would identify new and emerging educational needs, ensure

coordination of efforts, and maximize efficiency and effectiveness. The Department of Labor is to be commended for its Saving Matters retirement savings education campaign and its spelled specific components. This recommended review would seek to answer the question, are there additional educational needs not currently being met? In addition, primary research should be conducted to develop a greater understanding of the current behaviors, attitudes, and motivators surrounding retirement income. This primary research would provide a baseline understanding of the manner in which various demographic groups view lifetime income products and provide attitudinal [spelled phonetically] understanding by age, education, income level, race and ethnicity, gender and geography. Based on these two inputs, the review of existing programs and the primary research, my recommended next step would then be to design and develop and educational effort to address the outstanding communications needs.

In addition, I wanted to share a few thoughts on the millions of workers in the United States who do not have access to an employer sponsored retirement plan, many of whom are employed by small businesses. The recently introduced automatic IRA bills are a step in the right direction, and, in my view, deserve bipartisan support. If passed, it is highly recommended that an automatic IRA program be supported by an educational initiative for employers and employees. Currently those who lack access to employer sponsored retirement plans in larger numbers have unique educational needs, and these needs must be considered in developing an overall approach to delivering the retirement income education. These groups include but are not limited to small business owners, the self-employed, women, those living in rural areas, the geographically remote, Hispanics, and other race and ethnic audiences. These audiences need to hear about retirement income from trusted voices, those organizations and community leaders that have credibility with them. In conclusion, I would like to thank you for the opportunity to testify before you today. Retirement security is an issue of tremendous importance and the U.S. Department of Labor and the Department of the Treasury are to be commended for facilitating this critically important discussion. Thank you.

John Vine:

Good afternoon. I'm John Vine. I'm from Covington Burling. I want to join the others who have commended the Treasury and Labor departments for issuing the RFI, for holding this hearing, and most of all, for focusing on lifetime income issues. I've spent most of my career working on employee benefits for major employers. Today I want to present the perspective of major employers on issue number two in the agenda for this hearing, providing information on what will help participants make choices regarding the management and spend down of retirement benefits.

Based on the testimony presented so far, I'd like to offer three general observations and one spelled specific recommendation. The three general observations are, first, that the RFI identified an extremely important set of issues. Second, that there are a multitude of good ideas out there on what the Labor and Treasury departments might do to address those issues. And, third, given the voluntary nature of the employee benefits system, it is imperative that all parties continue to work together to address the issues. The challenge for the departments is where to go from here which brings me to my recommendation. That the labor department begin with the low hanging fruit -- by expanding interpretative bulletin 96-1 to cover distribution education as well as investment education. This is relatively easy to do. It can be done expeditiously. It's consistent with existing departmental policy. There's wide spread support for it as today's testimony indicates, and most important it will enable the department to leverage its authority by facilitating the efforts of employers to educate their employees and retirees on the value of lifetime income options.

Many employees don't understand what annuities are, or what the difference is between an annuity and installment payments. or how retirees can use annuities to address the risks that they will face in retirement. Other employees understand all this, but are concerned by the risks that annuities will present. The challenge is to help employees understand the risks they will face in retirement and to address those risks appropriately. All investments involve risk of one kind or another. Such as the risk of inflation, insolvency, longevity, morbidity, investment performance and emergency needs for liquidity. The challenge that retirees face is how to address those risks appropriately.

A number of major employers would like to act now, to help their employees and retirees get the most value out of their 401k plans. These employees are aware of the academic research on the value of annuities, and they would like their employees and retirees to be aware of the research as well so that they can make better informed decisions. But some employers are concerned that they will be sued for providing this information, that no good deed will go unpunished. Corporate managers ask why they should volunteer to do something they don't have to do if it might embroil the company in costly litigation, even if the litigation is meritless. They know that even meritless lawsuits can be very costly to defend. A department of labor regulation, interpretative bulletin or advisory opinion would go a long way toward addressing those concerns. There's much helpful information that can be provided consistent with interpretative bulletin 96-1, for example, the characteristics of fixed income annuities and fixed preferred annuities, the potential advantages and disadvantages of fixed annuities, research reports on the value of annuities, sources of information regarding fixed annuities and issue the names of issuers and marketers of fixed annuities. This information could be enormously beneficial to retirees for a variety of reasons. This is unfamiliar territory for many of them. The information is extremely important, and to many the employer is a trusted and unbiased source of information.

I recognize that there are many other things that the departments might do but this would be a sensible place to start, to begin with the low hanging fruit. That completes my prepared remarks. I'll be happy to respond to any questions the members of the panel might have. Thank you very much.

Male Speaker:

John, do you see any downside potential for the -- your suggestion or is it all upside, in terms of from our perspective?

John Vine:

From your perspective, I think it's all up side. I think -
- I can't think of an argument against providing information to employees about what they might do with the retirement savings.

[laughter]

Male Speaker:

So let's accept the proposition that there's a lot of information out there. Should in rethinking 96-1 we think about standards that -- of any kind that should be applied to the quality of the information or is it merely making information available?

John Vine:

Clearly, the information should be prudently selected, should be not misleading; it should be of high quality, but I think that's implicit in 96-1' it's implicit in what the department expects of plan sponsors; and I think that's what plan sponsors intend to do.

Male Speaker:

And obviously you believe that, to the extent that we clarify either by amending 96-1 or similar type of guidance, distinguishing that activity from investment advice or other fiduciary type of activity that employers will essentially take a more active role in providing this information. This probably goes to everyone on the panel.

John Vine:

The -- that's certainly what I would expect. I think many employers are anxious, actually, to provide the information. They're concerned about where the line is drawn between education and advise and would appreciate guidance from the department about where -- precisely where that line is.

Brooke Worden:

And I would say just to build on what -- what John was saying, that it's my belief that plan sponsors would do that, and I think plan sponsors want to do the right thing and want to provide the information, but I think in some cases they lack adequate support. And I think when we think about education, we should include plan sponsors in that mix in terms of additional education needed. I think we tend to go to the participant, but I think there needs to be additional education for the plan sponsor as well.

Tracey Flaherty:

I completely agree. The plan sponsors are getting these questions from their participants today, and I think they

could use some guidance in how they answer them and get educated themselves.

Male Speaker:

Ms. Flaherty, you talked about portability as a challenge, and certainly that is a challenge. Any thoughts that you have or things that you've seen that help to address that problem? I'm assuming you'd advocate more out of plan annuity options versus in plan options, but maybe you can just expand.

Tracey Flaherty:

I think you really have to look at both. I think plan sponsors really need the flexibility in plan design to address the composition of their workforce, and I think you have to look at options in plan and out of plan and options that allow you to go from participating in plan to out of plan if at all possible. Employees do not want to leave their -- for the most part, the majority of employees do not want to leave their retirement assets at their previous employer as they move from job to job. So I think providing the range of options along with the flexibility is very important.

Robert Doyle:

Okay. To follow on -- to follow on Michael's question in the relationship between in-plan versus out of plan options, John, do you imagine an expanded 96-1 to encompass information about the relative merits of in plan versus out of plan options, or your large employer's merely looking for clarity in providing information about in plan options?

John Vine:

No, I think most of them do not provide annuities or installment payment options under their defined contribution plans, so what I'm suggesting is that they provide information on they can do when they take the money out of the plan, roll it over, and then do what. And again, they're -- they're not going to be recommending that plan participants do anything in particular, but giving them enough information to decide intelligently and on an informed basis what's best for them.

Male Speaker:

Okay. As part of your -- your idea about education, you had mentioned the enhancement of benefit statements. Can

you elaborate a little bit more about what you see as an enhancement that would help in this area?

Tracey Flaherty:

Well, I think there are a couple of things. One is that I think using, to Brooke's comment and some others that we've heard today, using all of the communication channels that are available, online, social media, you know, all of the ways to engage participants in this education. And I think too -- for too long as an industry we've been focused on accumulation, and so investors -- participants get to be 60 plus, and they have this pot of money and there's a big behavioral issue about now parting with it to use in retirement. And I think if we provided more education on retirement income earlier in the retirement planning process, we would help get past that behavioral issue. And part of that is helping them translate their savings into some kind of a monthly income stream, much like we're all getting social security statements. And we have a sense of that not being just a lump sum at 65, but we have a sense of what it's based on and how it translates into a retirement income stream. And I think providing that context for why you're saving what the outcome is you're saving for is very important, and I think showing something on a monthly statement much like we've shown for years, you know, the accumulation dollars is really important. I haven't -- I don't have a recommendation on the methodology. That's really for others. But I do know from investor and consumer behavior that I think we need to provide more context of why you're saving and it's got to go through retirement not just to retirement because I think that's where we've been struggling to date -- getting more people to change their behavior.

Brooke Worden:

And I would love to see social media optimized more fully in terms of bring those 401k plan statements to life. I think a lot of time participants get those statements and they're very static or they have questions, and there isn't really a place for them to go to ask questions about that information, and I think social media is really a channel that we haven't fully tapped into in terms of delivering that retirement income education. I think, you know, to Tracey's point, that's something that the industry could really do more of.

Tracey Flaherty:

Well, it's interesting because it happens today in the work place, and you probably have heard anecdotes of, you know, the person -- there is usually a champion in the workplace who has no investment experience whatsoever, but is the one giving advice to all the employees at IBM. So I think there are some ways that you could do that in more organized basis to really provide the right information instead of this ad hoc investment advice, which is really what is happening today in the workplace in a lot of places.

Male Speaker:
Thank you very much.

John Vine:
Thank you.

Tracey Flaherty:
Thank you.

Robert Doyle:
With that we're going to take a short break.

[break]

Panel Seven

Robert Doyle:

With that I think we'll turn it over to our panel, and we'll start.

Rhonda Elming:

Good afternoon. On behalf of Aviva USA, I thank you for allowing us to appear at today's combined Department of Labor and Department of Treasury public hearing on lifetime income. I am Rhonda Elming, senior vice president of product management for Aviva USA. Aviva is part of the U.K. based Aviva PLC, the sixth largest insurance company in the world and a sales leader of fixed indexed annuities and fixed index life insurance in the United States. Based in Iowa and with offices in New York and Kansas, Aviva USA has approximately one million life insurance and annuity customers, and we employ nearly 1,500 people across the country. We can trace the presence of our predecessor companies to providing financial services in the United States to the late 1800s.

We understand the market downturn has created a shift in consumer attitudes towards retirement savings. This underscores the importance of planning for retirement with financial tools that offer lifetime income option. We have researched the marketplace and have spoken with our policy owners. As such, we know that consumer demand has increased for products that provide a safety feature of guaranteed lifetime income. Aviva focuses on the sale of annuities through independent agents, and as such, we do not currently offer our products directly through employer-sponsored plans. However, about half of our sales come from qualified annuities which are rollovers from employer-sponsored plans. This indicates a high level of consumer need for the solutions that our products offer and which cannot be obtained in an employer plan. These products primarily provide access to lifetime income solutions.

There are compelling reasons that access to these options within the plan would be efficient and valuable to consumers. However, very real barriers exist in offering annuities through these plans. These barriers prompted the Request for Information issued earlier this year and the need for today's hearing. Clarity on fiduciary standards, annuity portability, and disclosure of potential income streams from account balances are among the issues that

need to be addressed. We leave specific proposals to our industry colleagues and support the comments made by the American Council of Life Insurers, the committee of annuity insurers, and the financial services roundtable, all of which we are members.

If the obstacles to offering annuities in employer-sponsored plans were removed, Aviva USA and other insurers would be significantly more likely to enter the marketplace and provide consumers with products that need their lifetime income needs. It's important to remember that life insurers are the only private market solution that can truly provide lifetime income guarantees.

As mentioned earlier, Aviva USA is a leader in fixed indexed annuities and is a major issuer of qualified annuities. From our experience there are many reasons individuals are reluctant to elect receipt of their retirement benefits as a lifetime income option. Despite being around for generations, single premium immediate annuities, or SPIAs, have not gained widespread consumer acceptance. While a SPIA can offer a guaranteed lifetime income stream, it requires a large outlay of money while providing no account value in return. The consumer gets a promise of a future income stream but effectively gives up their rights to their asset and no balance appears on a monthly statement. In addition, a SPIA that guarantees income for life, offers no death benefit if the consumer dies prematurely. A SPIA also provides no flexibility to alter the amount received. If a consumer's circumstances change after purchasing a SPIA, for example, medical expenses increase or they experience a loss of other income, they have no ability to access their annuity. This is critical to understand. Many people do not annuitized because they lose access to their money. Going from a large accumulated savings balance to a stream of income with no visible balance or flexibility is a tough psychological prospect for consumers.

In addition to issues specific to SPIAs, all lifetime income options suffer from a general lack of consumer knowledge as to the amount of assets needed to support the consumer's post-retirement lifestyle. While financial experts generally accept a withdrawal rate of four percent per year from retirement assets to be sustainable for the length of one's retirement, surveys show that people generally believe they can withdraw between eight to 10

percent annually. The payout rates offered by lifetime income options, SPIA or otherwise, look unattractive against that overlay optimistic belief. Further, consumers don't fully grasp the long term effects of inflation upon their retirement assets and income streams and often don't factor in the erosion of their wealth and income over time. Therefore, a huge need exists for educating the consumer about the reality of paying for retirement, including both the length of time retirement assets must last and the income stream a certain amount of assets can support. Traditionally people underestimate how long they'll live and overestimate the value of a large lump-sum balance in providing an income stream in retirement.

Aviva USA's fixed income annuities are soundly placed in the middle of the market risk continuum. Like a traditional fixed annuity, an indexed annuity provides a guarantee of principal though with an interest crediting rate tied in part to the movement of an outside index such as the S&P 500. The benefit is a historically higher interest rate that provides a more effective hedge against inflation. Variable annuities, on the other hand, carry more risk. While the account value may appreciate more quickly, it is at risk. We believe indexed annuities to be the perfect compromise for a consumer seeking stable appreciation and affirmation that the money is there in the long term.

Aviva USA has been a leader in developing and using unique features on its deferred fixed annuities. For example, our optional income rider provides a valuable solution to common consumer concerns. Over 80 percent of our new customers have selected to add an income rider to their policy. They see the benefit in its design as it offers safety and stability through a guaranteed accumulation benefit that insures the policy owner has a minimum predictable base, guaranteed lifetime income payout rates that can double if the policy owner is confined to a nursing home or other qualifying facility, a death benefit option, flexibility to start and stop payments and continued control over the underlying policy account value. Income riders essentially allow customers to make periodic withdrawals while they maintain access to their annuities principal. This ability provides the peace of mind of lifetime income.

At Aviva USA we are in close contact with our customers and over the past 18 to 24 months, we have received hundreds of customer letters, some emphatically thanking us for offering annuities that were protected from the market crash. While many consumers lost an incredible amount of cash value in their plans, our products provided financial security and a guaranteed income stream.

We believe that lifetime income security is a pressing issue in the US and one that only financially sound life insurance companies like Aviva USA are qualified to administer, and we feel that fixed annuities play a role in every consumer's retirement portfolio, especially for those who cannot risk losing principal or cumulative returns. A recent study by Towers Watson found that insurers are increasingly focused on offering retirement income products through retail channels. We are a good example of a company doing just that. However while we currently focus on the retail marketplace, we do support regulatory changes that would allow consumers to have access through different distribution channels to [unintelligible] valuable products with guarantees offered by us and other insurance companies.

In closing, we are encouraged by hearings like this one which serve to educate the marketplace and create an open forum for exchanging ideas to improve both our performance and our customer's acceptance of the products we offer. I'm happy to answer any questions you may have, and I thank you for your invitation to participate today.

Paul Van Heest:

Good afternoon. I'm Paul Van Heest, and I'm the senior vice at TIAA-CREF, responsible for institutional product management. On behalf of my company, I too would like to thank the Department of Labor and the department of the treasury for convening this hearing which together with the request for proposal or for information earlier this year has set the stage for key reforms in the retirement planning arena. We look forward to partnering with the agencies on what we consider to be one of the most important financial issues facing all Americans.

By way of background, TIAA- CREF is the leading provider of retirement services for the academic, research, medical, and cultural fields. We manage over \$400 billion in retirement assets on behalf of 3.7 million individuals, and

we serve more than 15, 000 institutions, all not-for-profit. Our clients benefit from our more than 90 years of experience providing defined contribution pension plans to nonprofit organizations. This has given us a unique perspective on paying out lifetime income specifically from defined contribution plans. We currently pay more than \$10 billion in lifetime income each year to hundreds of thousands of retirees.

My testimony today will focus on three issues. First, I'll describe some of our participants concerns about choosing among lifetime income options and how we try to help them alleviate those concerns. Next, the management of our clients' experience in the spend-down period, and finally the importance of disclosing retirement accumulations in the form of a monthly income stream on participants' statements throughout their careers.

When plan participants begin considering the transition into retirement, they're often faced with a number of difficult financial decisions. One of the most challenging is how to convert their nest egg into an income that will last them for the rest of their lives. Some of the concerns that our participants often raise are, "How much income will retirement savings produce? What are my options for receiving income? And which options are best suited for me and my family? And how can I structure my income so that it will not only last but grow throughout my retirement years?"

TIAA-CREFF offers a number of resources to help meet our participants' retirement planning needs. These include personalized one on one counseling sessions with TI - CREFF's non-commissioned consultants either over the phone or in person. Literature that provides insights on retirement planning and explains income options -- an interactive online planning tool such as lifetime income illustrations. Our overarching goal is to make sure we address all our participants concerns early in the process, well before they need to make an income decision, so that when it's time to execute their plan, they'll feel confident that they're making good decisions. From our perspective this starts with a recognition that there's no one size fits all solution. Each individual situation is unique and accordingly, TIAA-CREFF offers our participants several different options for structuring their retirement income to meet their own unique needs. So we stress

individual choice and believe most retirement situations actually require multiple solutions. But we also believe that one of the most effective and efficient ways to address concerns about preventing shortfalls in retirement is through a guarantee income life annuity.

Unlike most 401k plan participants, our clients have annuities available directly through their employer-sponsored plans in both the accumulation and income stages of retirement. We believe that offering low-cost annuities during the accumulation stage actually helps to address and to alleviate participant concerns about lifetime income. It does this by recognizing all through their careers that they're saving not just to accumulate wealth, but also to ensure they'll receive an adequate income in retirement, rather than suddenly being faced with the concept of lifetime income at this already stressful moment in their lives.

We found also, both in research and in practice, that this focus on retirement income has a positive influence on the decisions that clients make on retirement. A recent study by the TIAA-CREFF institute found that retirees that have annuitized their retirement savings are more than twice as likely to have used an annuitized -- to an -- annuity to save in a defined contribution plan while they were working as compared to those retirees who opted not annuitize. This study was not limited to TI -CREFF participants but our own experience indicates that nearly 1/3 of those that begin taking an income stream with TIAA-CREFF do select a life annuity.

Transitioning into the spend-down period is a process that is often very challenging for individuals entering their retirement years. Many people focus on the accumulation of long term savings but the management of income and retirement doesn't receive as much attention as it deserves. Participants have to make difficult decisions choosing from a variety of options and often with less guidance than they had while in the accumulation phase. The easier course of action is just to take a lump sum payment. But this often refers in simply deferring these decisions. Since retirement income may come from a variety of places it's important to take a complete inventory of all forth coming sour-- income sources including social security, defined benefit pension plans and employer-sponsored DC plans, IRAs, and personal savings.

Participants considering lifetime income annuities should understand that it's not always necessary or required to use all of one's retirement savings when purchasing an annuity. For this reason, TIAA-CREFF not only allows for partial annuitization but we believe in most cases an annuity stream based on only a portion of retirement savings is the preferred option to meet a participants needs. We counsel our clients to purchase a guaranteed annuity that will prefer the necessary level of income to cover their basic expenses like food and housing. There are a variety of vehicles that are well suited to help individuals manage additional discretionary costs and we encourage them to consider their health, expected longevity and other potential limitations on retirement income before making a final decision on a spend-down plan.

Another important approach is to increase awareness by providing participants with a regular statement that offers two distinct views of their position in the plan. One showing their accumulated balances and a second that illustrates the income they can expect to receive in retirement. Current law requires that plan participants receive regular statements that provide a summary of their current accumulations. While these statements are an important tool in keeping participants informed and engaged in their retirement goals, providing only account balances can have the adverse effect of encouraging individuals to view their retirement savings as an amount to be withdrawn in a lump sum rather than as a stream of income to provide lifetime financial security. Depending on need, either or both of these views may be valid, and therefore we believe it's important to show both.

In fact, TIAA-CREFF began providing our participants with income projections on a regular basis in the early 1960s. Currently, we include an illustration of potential retirement income on the first page of all of our participants quarterly review statements. This view uses certain assumptions to show what participants monthly income would be in the future. While we don't view this as a silver bullet to changing the way people view their retirement savings, it allows participants to become familiar with the concept of a lifetime income stream earlier in their careers. It also allows us to have meaningful conversations with participants about lifetime income, provide them with more detailed information and

direct them to other resources such as those on our website. This can help them to make more informed decisions both today and in the future achieving the goal of receiving adequate income and retirement rather than focusing solely on building wealth. While the anecdotal feedback we received from our participants on this feature has been positive, a recent ACLI survey of DC plan participants found that more than 85 percent of respondents expressed an interest in having this type of information available on their regular retirement statements or on a secure website. And 60 percent said that if such an illustration revealed that their income in retirement would be inadequate they would begin saving more immediately. In an environment where we're all trying to encourage greater savings for long term needs, this reason alone provides an important incentive to such an illustration. Along these lines, we support current proposed legislation that would require all retirement plan participants to receive at least annually, an illustration of how their current accumulation would translate into income at retirement. However, we believe that plan providers should take action now to institute this feature rather than waiting for a government mandate.

In conclusion, we believe that the integration of annuities into defined contribution plans is a key component to improving retirement security for all Americans. We encourage the agencies to take steps to make it easier for sponsors to include them in retirement plans. We commend the agencies for continuing to bring attention to this very important issue and appreciate the opportunity to share our perspectives with you today. We hope that as you continue this process you'll consider TIAA-CREFF a partner in this effort and look to us to provide input based on the unique perspective we have developed through providing lifetime financial security to our clients for more than 90 years. I look forward to taking your questions.

Robert E. Sollmann:

Good afternoon everyone. My name is Bob Sollmann, and I am the executive vice president responsible for retirement products at MetLife. MetLife commends the agencies for issuing the RFI and holding these hearings, and we thank you for inviting MetLife to testify and share our experiences with you.

Why is guaranteed income so important? The longevity risks faced by an individual is far more significant than the investment risks faced at retirement. While individuals can manage both market and inflation risk by changing their investment strategy, they cannot accurately predict how long they will live nor can they recreate the benefits associated with mortality pooling in terms of that pool's ability to maximize income on their behalf.

MetLife believes there are five areas in which the agencies should take action. Education and advice, partial annuitization, alternative designs, annuity illustrations, and the fiduciary standard.

Let's talk first about the ability to provide information whether that's education or advice that will help participants make decisions about managing and generating retirement income. MetLife's eighth annual employee benefits trends study showed that 49 percent of those who have a retirement nest egg are interested in protecting their retirement income, 40 percent are interested in learning how they could use annuities as part of their defined contribution plan, and 44 percent would like their employer to offer an annuity option. When they retire, 55 percent of workers told us that they'd prefer to receive part of their nest egg for as long as they live rather than taking it in a lump sum.

Why then do so few employees elect annuities when they're available? They're simply overwhelmed by what they don't know. They have a number of questions and for starters, what is an annuity? And overwhelmed by all of the unknowns, employees often do nothing to create a sustainable lifelong stream of retirement income. Our research tells us that people are more confused than negative about annuities. This confusion, I think, underscores the need for education that we've all been talking about. When education and advice about distributions are provided, especially through the workplace, participants show that they're hungry for the information. MetLife's retire wise program is an employer-sponsored workplace retirement planning seminar offered by over 500 employees today, nationally. Approximately half of the employees who attend those seminars go further to request the complimentary face-to-face consultation to gather information for -- for their specific situation. The success of this program -- the success of retire wise

demonstrates that employers are seen as a trusted source of information on retirement and that, indeed, employees are hungry for that information.

The Department of Labor has done excellent work in providing guidance on how plan sponsors can effectively provide participants with education and advice regarding the accumulation phase. This can be effectually built on by extending the guidance to the distribution phase. We should give employers the same choice -- provide education regarding distribution principals without fiduciary responsibility or providing advice regarding specific distribution options with fiduciary responsibility. Interpretive Bulletin 96-1 which many of us have talked about prescribes how employers can provide participant education with respect to investment allocations. The next logical step, it seems to me, is to provide guidance clarifying what education may be provided about the distribution face without triggering fiduciary responsibility.

Some plan sponsors will want to provide individualized distribution advice. The SunAmerica Advisory Opinion has led to broad use of computer models based on generally accepted investment theories. The DOL can build on this success by issuing SunAmerica-like guidance for the distribution phase.

Now I'd like to turn to our second topic: partial annuitization. Education and advice are absolutely critical, but alone they are not enough. The agencies need to do more to enable participants to receive some level of guaranteed lifetime income. Today, here's what typically happens. When a participant retires, if they're fortunate enough to even have a guaranteed income option, they're often presented with an all-or-nothing option, an all-or-nothing choice. And not surprisingly, they don't annuitize the entire balance. From the individual's perspective, purchasing an annuity with a portion of the assets -- a portion of the assets helps to minimize the negative effects of a large one time purchase to better achieve that balance between liquidity and lifetime income. When participants have the opportunity to partially annuitize, they do so in greater numbers than when total annuitization is their only option.

Our own experience with the federal government in fact underscores this point. MetLife has been the exclusive provider for the federal thrift savings plan -- the TSP -- since the plan's inception, 20 years ago. And when the plan first began the annuity was an all or nothing option. In 2004, the plan was amended to include partial annuitization and as a result the TSP saw an immediate and dramatic result: a 60 percent increase in the number of participants annuitizing some of their balances. The agency should provide enhanced education to plan sponsors about their annuity -- to offer partial annuitization.

Our third topic relates to emerging annuity products, some of which are offered as an investment alternative in plans and others as plan distribution options. Products offered as investment alternatives have several important advantages. First, they allow participants to systematically purchase amounts of guaranteed income, avoiding that intimidating big purchase of retirement I talked about a moment ago. Second, purchasing annuities over time helps manage interest rate risk, the risk of buying when interest rates are low, the investment equivalent of dollar cost averaging. And third, the availability of these products helps participants view their plan in terms of future retirement income and not just distribution -- not just accumulation.

To stimulate the offering of these annuity products, we recommend the DOL consider revising the QDIA regulations to require QDIAs to contain an in-plan accumulation annuity component. Target date funds and managed accounts are important tool in preparing an individual for retirement, but these funds focus exclusively on accumulation and don't prepare individuals for the arguably more challenging, distribution phase.

Another emerging and equally as powerful solution to creating lifetime income is the use of longevity insurance, a deferred fixed income annuity that can be purchased at retirement or earlier. The biggest challenge in retirement income planning is predicting a date of death or what is known as the planning horizon. Because longevity insurance payments don't generally begin until age 80 or 85, average life expectancy, retirees can then manage their assets to a set time horizon, turning uncertainty into certainty. This has the added benefit of helping individuals to neither over or under spend. There's just one problem. The RMD

rules, the required minimum distribution rules, effectively preclude offering longevity insurance within RIAs or qualified plans, and we recommend changing those rules to exempt longevity insurance acquired within qualified retirement plans or RIAs from the RMD requirement.

Moving to our fourth topic -- one of the very important ways in which we can help participants make the shift in mindset to retirement income is to show them, as many have mentioned, on a regular basis, on their benefits statements, how much guaranteed income their defined contribution assets can generate. We believe this will prompt workers to increase their savings. This information should be provided so that it is clear, so that it's understandable, and employers should have a simple means of compliance that doesn't expose them to fiduciary liability.

The final issue we believe the agencies should address is the fiduciary standard. Plan sponsors who want to offer annuities in their DC plans need clear guidance on selecting an annuity provider. Plan sponsors tell us that their revised regulatory standard is helpful but not enough. At a meeting in April -- this past April with 20 of our largest institutional customers, we talked about this issue. Plan sponsors said that they are concerned about the potential of being sued for trying to do the right things for their employees. They told us that their decision to offer annuities in their plans will turn on this issue. We hear this day in and day out in the marketplace. As the AOL -- as the DOL considers how best to address this concern, we'd love to help you.

In closing, while it may be possible to manage lifetime income in the retail market, employers are expressing interest in helping their employees achieve lifetime income security, and as I said earlier, employees are increasingly asking for this to be available in the workplace. Without appropriate legislative and regulatory guidance in this area, we believe that plan sponsors will not act in sufficient numbers to give their employees an opportunity to create guaranteed lifetime security from their defined contribution plan assets.

Again, on behalf of MetLife, thank you for your time, and I look forward to your questions. And just before I turn it over to the panel, for the record let me clarify the level of protection available through state guarantee funds --

this came up earlier in the morning. The levels do range, as was said, between \$100,000 and \$500,000 but the NAIC, the National Association of Insurance Commissioners, has a new model statute that increases the minimum of that range to \$250,000. Thirty-three states today have adopted that new minimum \$250,000 level. Thank you.

Robert Doyle:
Thank you. Questions?

Male Speaker:
Well, starting with the -- your last point first, I have questions for all of you on two separate topics -- now three topics based on your last observation about state guarantee associations. I have heard recently that there is a bit of confusion regarding the extent to which -- what you call the accumulation type annuity -- the in-plan annuity -- the extent to which those annuities are covered under guarantee association protections. Could you speak to that, please?

Robert E. Sollmann:
The whole field here is that it's a very complicated area, and there's a lot of detailed information that bears on these points. These new products that are being offered in the marketplace are the type you described -- in-plan accumulation annuities, variable annuities with living benefit features -- are an area that we need to consider carefully in how these provisions apply, and I'd be happy to, you know, sit down with you separately with our experts to go through that in more detail later.

Male Speaker:
Okay. Okay, in terms of amounts -- a different question, still on coverage -- the extent to which those kinds of policies are covered -- in the group arrangement setting, is it your understanding that the \$300,000 -- as an example, the \$300,000 limit applies to the group contract or the individual certificates of annuity? Which is the policy holder -- the plan participants?

Robert E. Sollmann:
It's my understanding it's at the individual level.

Male Speaker:
Okay. Okay. All right, focusing on the in-plan annuity products, earlier today, a number of different witnesses

raised the issue of portability and all three of you are strong advocates of including the accumulation annuity products in plans. Would you react to the problems earlier, the problems mentioned earlier by those folks who say that portability is an impediment to having them in plans?

Paul Van Heest:

I'll start. I think within the not-for-profit arena there's been a greater degree of retention within plans, I think than certainly than in the 401k world. And one of the reasons was that TIAA-CREFF was actually founded to promote portability, so the contract structures that were designed were intended to be -- to facilitate portability from plan to plan. I think what's happened over time with the introduction of IRAs and other advances over the many years that the TIAA-CREFF contracts have been there is -- need to be able to establish portability in different ways. So one of the things that we've tried to do now is to facilitate from -- both between plans but also from the retirement plan to the IRA product. And some of our contracts actually allow you to maintain your specific vintages and the accumulations that you've built up and all the benefits therein by moving to IRAs, particularly some of the newer contracts and what we're trying to do is to facilitate that portability because it's increasingly an issue.

I think there's also a need for portability between vehicles so as retirement plans now offer both mutual funds and annuities, there's much more ability to move from an annuity into a mutual fund and then to roll into an IRA. So I think that while I understand some of the concerns that were raised earlier, I think our experience at TIAA-CREFF has been that there's a lot of retention within the plans in terms of the annuities. We've found that people who stay within the plans tend to be more likely to annuitize in many cases, rather than people who move into an IRA who don't necessarily annuitize as frequently. So, I think there are a lot of benefits to maintaining within the retirement plan, but I also think that portability's an important issue, and I think there's a psychological issue where people want to feel like they have the ability to move if they should choose to.

Robert E. Sollmann:

You know, I would just add that I think that some of this is a function of how robust the current market is for some of these products. And I think as the market develops, particularly if some of the work that comes out of these discussions serve as a catalyst for the development of that marketplace, I think any number of these issues including the issue of portability, will be much more quickly addressed.

Male Speaker:

Okay. I'll let that digest because I'm not sure that completely makes sense yet to me, but maybe we'll come back to that. And we'll switch to the other topic, please and that's the use of benefit statements and the -- I guess it was Mr. Van Heest, you said that since '60s you have been doing this on benefit statements and you've been projecting --

Paul Van Heest:
[assent]

Male Speaker:

-- the balances and can you quickly mention the assumptions that you use when you project somebody's account balance at retirement and specify whether -- when you're projecting are you projecting a person's current account balance and the stream of income that balance will purchase immediately or at a retirement date that is projected in the future?

Paul Van Heest:

We're actually projecting based on an assumption of ongoing contributions at the current level with the same allocation that's currently used for allocation with a three percent annual growth rate with an assumption of a single rate annuity at age 65 with a 10-year guaranteed period now and an assumed interest rate of four percent. I think what we try to do with these illustrations on the statements is to view those as a starting point for a conversation rather than the end point, and we try to emphasize that in our counseling sessions, in our seminars. These assumptions are and this -- I heard this discussion at one of the earlier panels -- it's impossible to come up with a set of assumptions that applies to everyone because everyone's needs are so different so the goal here is to try to get people to start thinking this way but then to interact with counselors, interactive tools, et cetera to begin to

better understand that, and we do find that we get a lot of phone volume when those statements come out because people want to begin to discuss and understand that more.

Robert Doyle:

Just to kind of follow up along on that same line in the earlier discussion --

Paul Van Heest:

Sure.

Robert Doyle:

--I think I'd be interested in each of your reaction to that earlier discussion about standardized methodology for doing these types of calculations -- whether that's a good thing, bad thing?

Paul Van Heest:

I'll start and then I'll [unintelligible].

Robert Doyle:

Should it be simple, complex, but --

Paul Van Heest:

I mean, I think --

Robert Doyle:

-- something that's uniform.

Paul Van Heest:

Sure. I think that one size fits all is awfully difficult. At the same, there's got to be some boundaries. I don't know if it's a few different acceptable alternatives, but I think that because a lot of the annuity products that are out there in plans can be different from one another, to have a single set of assumptions can at times make it more difficult to do anything except, potentially, to compare the income stream you might get from different products. But for the most part, retirement plans only have one fixed annuity in them so you're not going to necessarily have -- it's not like you're choosing which product to use, it's more to try to get a sense for what the value of that is in retirement.

So I would suggest that you think about some different alternative and with some degree of flexibility that as long as broad guidelines are used to make them useful to

participants and, again, to really make them a -- emphasize that they're a starting point because I think the real danger in doing this, if it's done as the end result, is that people begin to have expectations that get locked in as opposed to having dialogues about this.

Robert E. Sollmann:

I mean, in my opinion, this is a case of, you know, one small step for man and one giant leap for retirement income.

[laughter]

I think that we -- there's a risk that we try to overcomplicate this. Think about what the objective is here. The objective is education and presenting that in as simple and clear a means as possible, I think, will help employees understand what their options are in terms of converting their assets into income and also to begin to think about the challenges of converting and saving more and the challenges of converting their assets into income.

The other dynamic here is the plan sponsor community and I think we want to construct something that is embraced by the plan sponsor community and I would argue that the more complicated we try to make this, the less the plan sponsor community will embrace the need to do this and the accept -- and the -- and to understand that it really needs to be required on these statements. So I'm an advocate -- we're an advocate for applying this to current account balances, having standardized assumptions that we all adopt that are set by the Department of Labor and having that serve as a safe harbor. And I think that will lead to wide adoption and acceptance of this.

Rhonda Elming:

At Aviva USA, we understand that education is of utmost importance and that when someone is looking to annuitize their account balance there isn't "a" answer but rather a range of answers depending on how their funds accumulate, depending on when they elect to take a lifetime income, et cetera. So I believe that there needs to be enough flexibility in any standards that are put forth to allow the plan sponsor to be able to project for the products that are offered within the plan and also to help educate the plan participants. If they have the flexibility -- let's say they have an online tool as opposed to a

statement with something provided to them in writing where they have the flexibility to change certain assumptions to understand how those assumptions may impact their lifetime income, that provides a lot more value in terms of them really understanding the situation that they're in and the risks that they face.

Robert Doyle:

So, just again to follow up a little bit -- so, if we took a safe harbor approach similar to that that Sollmann laid out, and it was a safe harbor, it wouldn't necessarily preclude alternative approaches?

Rhonda Elming:

But at a minimum require that a certain level of projection is available to aid consumer understanding?

Robert Doyle:

Well, require, not require but if you did it, at least for Department of Labor purposes or Treasury purposes, whatever, it would be an acceptable means and permissible means without liability, whatever that means in this context.

Rhonda Elming:

I think that would be very helpful, yes.

Male Speaker:

And then if I may, it's just -- one more to follow up on that, sort of, safe harbor and the standard assumptions, what do you -- are there -- for purposes of interest rate and mortality rate assumptions, what does MetLife suggest is appropriate in this context?

Robert E. Sollmann:

Well, in fact the PBGC publishes annuity rates today, commercially available annuity rates that they aggregate through a survey, and it seems to me that there's an opportunity to leverage that. It's available today and have that as the standard that provides that safe harbor that everyone adopts.

Male Speaker:

Would the 417 applicable interest rates be a viable alternative?

Robert E. Sollmann:

Not sure I understand the question.

Male Speaker:

To the PBGC interest rates, are the code 417(e) [spelled phonetically] applicable interest rates something that also could be used?

Robert Doyle:

I don't everyone has their code with them today.

[laughter]

Male Speaker:

Maybe if he wants to translate that.

[laughter]

Male Speaker:

That's part of the offline discussion that we could have.

Female Speaker:

This is a defined contribution plan audience. You're talking in DB terms.

Male Speaker:

I'm just looking for an interest rate.

[laughter]

[low audio]

Female Speaker:

That it -- under a defined benefit plan, if somebody's going to take a lump sum there are certain assumptions that have to be used to determine what the minimum lump sum is and post-PPA, the interest rate is -- it's actually like the segment rates and if -- I'm not about to launch into an explanation of the segment rates -- it's either you understand or you don't, I think, or you recognize the reference or you don't -- so that's it. But the idea is to, you know, it sort of looks over the stream of income or, you know, the period over which the payments would be made so there's a set of interest rates that would apply based on that period. And just to -- historically, I think it was before the 94 that the PBGC rates were used and then there was a Treasury -- a 30-year Treasury rate, and now we have --

[low audio]

[laughter]

Female Speaker:

Actually, are we out of time or do I have time for a question? Actually, Ms. Elming, I wanted -- you mentioned when you were talking about Aviva USA, you mentioned that about half of the sales -- annuity sales -- are from -- you used the term qualified annuity -- that they're from -- via rollovers from employer plans. So is that -- do they -- is that then just like an annuity product or is it in the form of an IRA?

Rhonda Elming:

It's an IRA. We issue it in the form of an IRA so it would be subject to required minimum distribution rules, et cetera.

Female Speaker:

And do you have any sense as to who are more likely to do that? Is it people at retirement age or is it people, you know, terminating employment at younger ages who are just taking their money from the plan? Do you have any sense of that?

Rhonda Elming:

I would say that the average issue age of our policies is around age 65 --

[chime noise]

-- so it's generally people that are closer to retirement that are purchasing those.

Male Speaker:

Oh, just a quick question because we're out of time, but just from the school of best practices, within your own retirement plans, do you see a lot of employees adopting, using, annuities, partial annuitization within your own plans? When you think about your own plan design, do you guys have a design within your own plans for your own employees that you think would be helpful in terms of insights surrounding this question, to get people to use annuities more comprehensively?

Paul Van Heest:
Can I go first?

Female Speaker:
Go ahead.

Paul Van Heest:
We actually offer TIAA-CREFF annuities to our employees,
and our employees are required to annuitize out of the main
retirement plan.

[laughter]

Not out of the supplemental plans but out of the main
retirement plan -- out of the employer funded plan.

Male Speaker:
Okay.

Robert E. Sollmann:
And we offer an annuity option in our defined contribution
plan, and we have found, with a real focus on education,
that the participation levels -- [unintelligible] -- quite
strong. But I think the most striking evidence that we
have is when I mentioned in my testimony -- the Federal
Thrift Plan has just been just a remarkable turnaround.

Male Speaker:
Okay. Can I ask one follow-up question on the partial
annuities? A couple of you talked about that as being an
important perhaps solution. But I don't think any of you
mentioned any kind of particular problems relating to
partial annuities that, you know, the government could help
with. Is there anything in particular that is problematic
with regard to offering, you know, partial annuities?

Paul Van Heest:
I don't know that we've found specific to partial annuities
that there are problems. I think some of the things that
Bob talked about in terms of just making it easier for the
plan sponsor to get comfortable with annuities overall is
more the place that we would see some real opportunity
rather than the partial annuities themselves.

Robert E. Sollmann:
I think there's an opportunity for the agencies to help
educate plan sponsors on the value and the effects that

partial annuitization could have and, of course, we in the industry can help in that, you know, move that conversation forward as well. I think the question is if there is then real inertia there, do we need to go further than that. Do we need to consider incentives to encourage employers to offer partial annuitization or do we need to go so far as to require that if an annuity option is available in the plan that partial annuitization has to be required as part of that design.

Male Speaker:

Just one very small clarifying question since you mentioned the turnaround in the thrift plan that when partial annuitization was offered, I think you said 60 percent increase in take up. Sixty percent like from what rate to what rate?

Male Speaker:

Anybody in the audience?

Female Speaker:

You know, we don't actually have the annuitization rate by agencies, but I think what's important to note is the 60 percent figure that -- that Bob mentioned and even more interesting than that was the average purchase amount increased dramatically because people who had higher balances were now not forced --

Male Speaker:

Okay.

Female Speaker:

-- to annuitize but they also felt the need to have guaranteed income but because they had, you know, more money, they couldn't -- they didn't feel that they wanted to take advantage of it. So I think those two combined really shows the power of [unintelligible].

Male Speaker:

Okay, because that was my second question -- what about the amounts -- but I mean, a 60 percent increase could be from one percent to 1.6 or from something much higher, so -- but we can get those data separately.

Male Speaker:

Sure.

Male Speaker:
Thanks.

Robert Doyle:
Any other questions? Okay, I thank the panel

Robert E. Sollmann:
Thank you.

Paul Van Heest:
Thank you.

Panel Eight

Robert Doyle:
Welcome.

Male Speakers:
Thank you.

Robert Doyle:
We'll leave it to you as to how to proceed. You can go with Mr. Hess?

Donn Hess:
All right. Well, good afternoon. I'm Don Hess, and I lead product development for JP Morgan Retirement Plan Services, a division of JP Morgan Asset Management. I'd like to thank the Department of Labor and Department of Treasury for sponsoring this hearing on the very important topic of retirement income for Americans.

We at JP Morgan Asset Management share your concern and have been working with plan sponsors and participants for the last 20 years to help individuals insure that they meet their retirement goals. We have been at the forefront of many developments on behalf of participants and we look forward to participating in that chapter of innovation.

For this hearing my comments concentrate on three broad areas: participant communications, disclosure of account balance as an income stream, and industry innovation with respect to retirement income products. Beginning with -- pardon me -- beginning with retirement plan participant communications, we see different levels of participant engagement depending on both financial complexity and life stage. For the majority of participants, managing daily expenses is the top financial priority so long-term planning tends to take a backseat. There are inherent differences in the thought processes, motivations, and behaviors associated accumulation of assets versus deaccumulation or the distribution of assets.

During the accumulation years, we hear very little from participants. Only 25 percent will call our service center, and only 1/3 will visit the website more frequently than quarterly. More than two out of five participants won't contact us at all. At deaccumulation this changes. Eighty-six percent of exiting participants call our service

center, and 68 percent of them call multiple times. When it comes time to translate accumulated assets into income at retirement, participants change their behaviors. They look for trusted guidance.

Assistant Secretary Borzi noted in her testimony before the Senate Special Committee on Aging's Hearing on Lifetime Income Options for Retirement, "Public policy initiatives have primarily focused on the accumulation stage of retirement planning. Only recently has there been a greater focus on the deaccumulation stage of retirement and what workers and retirees do upon receipt of their retirement savings." We agree and believe the industry has similarly focused participant communication efforts on accumulation.

Much of this focus is entirely understandable. Primarily because only recently has 401k plans become a primary source for retirement income. Widespread adoption of 401k plans began in the mid-1980s and as a result, only now are participants retiring with more than 30 years of accumulated savings. So, to date, it has been appropriate to focus on helping participants define their goals and monitor their progress accumulating assets in pursuit of those goals. Education or products to manage the spend-down of retirement savings couldn't overcome an insufficient account balance at the time of a retirement. Or said another way, we could make \$1,000 less for 25 years, but no one would be very happy with the results.

When participants reach the retirement milestone, however, we have found that the availability of education does make a positive difference. In 2005, JP Morgan initiated a program to address the issue of premature cash-outs by promoting the availability of retirement consultants, specially trained to discuss the implications of distributions from qualified plans. Five years since its inception, terminated participants are now 41 percent more likely to retain the tax deferred status of their retirement assets.

We have learned from these retirement consultants that participant engagement at retirement increases for two specific reasons. First, their retirement is a current, tangible collection of assets rather than a more nebulous future benefit. Second, and more importantly, the

decisions they must make about those assets are very complex.

A number of factors come into consideration when planning the spend-down of retirement savings. Among these are sources of savings outside of the plan, additional sources of retirement income, marital status, presence of children and overall health of the participant. In addition, it should be understood that the spend-down of retirement savings is not a straight line but rather a u-shaped curve. Retirees may draw more heavily on their savings in the years immediately after their retirement to enjoy travel or recreational activities. As they age, spending may decrease till their later years when medical expenses again require a greater draw down of savings. These factors increase the complexity of managing retirement savings over and above what we experience in educating participants during the accumulation stage.

The next area I wanted to address is the disclosure of participant account balances as an income stream. We have been vocal proponents for this for more than 10 years. In fact, since 2002, we have proactively provided participants with their annual retirement income in today's dollars and displayed this number online, on statements and over the telephone. This practice gives participants context for their accumulated balances. For example, communicating to a 45-year-old living on \$80,000 a year that he is tracking towards \$78,000 a year in retirement presents a picture. Communicating to that same 45-year-old that he is tracking toward \$35,000 a year in retirement presents a very different picture.

By consistently incorporating this type of information, we have seen participants take positive action to improve their income replacement in retirement. From March 2005 through June 2010, we have seen an overall increase in income replacement of 12 percent and an increase of 36 percent in the number of participants on track to retire comfortably. This movement occurred in an essentially flat market. The Department of Labor and Department of Treasury specifically asked about whether a statement number should look forward. We categorically believe that it should. In a recent study by Morgan, nearly one in four Americans said they had no idea how much of their current income, their existing savings could supply in retirement. Showing an account balance to an annual income in retirement gives

participants a realistic and comprehensible perspective. This is important because, in the previously study, nearly 70 percent of participants admitted to not reading the plan information they currently receive. A simple and direct way to show the future value of current savings is an important consideration in communicating with participants.

That being said, we hesitate to encourage legislation or regulation that mandates a one-size-fits-all formula. We believe any regulatory or legislative mandate should set a minimum of what needs to be provided with flexibility for providers to go above and beyond that minimum. We say this because there are a number of different providers in the industry, their capabilities vary and income projection calculations must be complex enough to include all known sources such as social security, defined benefit plans and other holdings. In addition, plan types and designs vary and can add to the complexity of calculating a projected balance at retirement.

It must also be understood that projections based on a single plan may not provide a complete picture of a participant's potential retirement income. As workers change jobs, they may have considerable retirement savings outside of their current plan, especially considering the medium employment tenure of just over four years, according to the Bureau of a Labor Statistics data. And finally, any disclosure mandate must include relief for plan fiduciaries and service providers to prevent liability from income projections being misinterpreted as income guarantees by plan participants.

The final topic I would like to touch on is industry innovation with respect to retirement income products. Today there is no lack of proliferation of retirement income products. Options range from retirement income through advisory services, annuities, in-plan retirement options, and target date funds with [unintelligible] to account for through-retirement solutions. If I may be allowed to mix metaphors, there's no silver bullet for retirement income. Given the complexity of retirement needs I described earlier, what is most effective is a quiver full of arrows. In her testimony before the Senate Aging Committee, Assistant Secretary Borzi posed the question of whether the regulation under Section 404(c) and the qualified default investment alternative regulations should be revised to encourage the inclusion of certain

lifetime income products. It is our belief that this would be premature given the ongoing innovation and product development presently occurring within the industry.

For example, in-plan annuities have received some attention of late. While these products may be useful for some participants, we wonder if they are suitable for all. We've examined our own participant base and focused on participants close to retirement -- those over the age of 55. Many have not accumulated sufficient account balances to adequately use in-plan annuities while simultaneously maintaining some level of liquidity. We believe this is because many have not had the opportunity to participate in a 401k plan long enough to accumulate sufficient balances. For these participants, annuity solutions outside of the qualified plan were assets for multiple savings vehicles [unintelligible] consolidated may make sense. Inside the plan, advisory solutions that come with a lower cost and more flexibility may make sense.

In contrast, we have likewise considered annuity products for younger participants, those under the age of 35. The additional cost of the guarantee on in-plan annuities for these younger participants whose primary goal should be accumulating as much retirement savings as possible may put a drag on long time returns. Indeed, some of these products recognize this and limit access to participants over the age of 50. For younger participants, traditional accumulation products seem to make more sense. On the other hand, participants currently in the 35-to-45 age range will have had more of an opportunity to accumulate account balances than their existing 50-plus colleagues as they approach a near retirement time horizon, it may be appropriate for them to consider paying for an annuity guarantee.

All of these thoughts can be debated but the point is, with such a variety of suitability issues, it is difficult to identify any one retirement income oriented solution that would be appropriate to use for a qualified default alternative for all parties. Even beyond the question of suitability, the costs associated with any sort of guaranteed income solution present fiduciary challenges from selection, monitoring and portability perspectives.

Given these challenges, we ask the industry be allowed time to innovate. As mentioned earlier, key accumulation

features such as automatic enrollment and escalation were developed in the industry. Today they are common design features that are recognized and encouraged by the Department of Labor as prudent practice. We are proponents of income replacement projections, communications that explain retirement income and relief for inclusion of income products in retirement plans. We believe, however, that the industry needs time to innovate in each of these areas. We ask for guidance that provides the fiduciary relief to encourage innovation without mandates or revisions to the 404(c) and qualified default investment alternative regulations that might limit the potential solution set. The industry is exploring a number of possible tools for participants during the deaccumulation stage. Thank you for your time this afternoon, and I welcome your questions.

[laughter]

Christopher Jones:

Good afternoon. I'd like to first of all thank the Departments of Labor and Treasury for the opportunity to provide testimony at today's hearing. My name is Christopher Jones. I'm the executive vice president of investment management and chief investment officer for Financial Engines. We're a leading provider of investment management and advice to participants in retirement plans.

Financial Engines is the largest independent registered investment advisor of America with advisory services to more than 7.4 million plan participants. We also provide discretionary professional management services to more than 443,000 participants at 385 large employers across the country. Our 12 years of experience in providing advisory services to millions of employees have given us insights into the lifetime income preferences of both participants and plan sponsors. In addition, over the past four years, the Financial Engines Retiree Research Center has conducted extensive research on the economic and behavioral issues associated with lifetime income, publishing a number of papers in industry and academic journals. Through our research we have conducted many hundreds of individual interviews to better understand what plan participants want and prefer in a lifetime income solution.

In my testimony today, I'd like to focus on three key points. Number one, defined contribution plans must play a

primary role in helping millions of working Americans achieve lifetime retirement income. It is critical that the government provide appropriate protections and incentives for plan sponsors to offer the help that the participants urgently need. Number two, workable lifetime income solutions for defined contribution plans must offer substantial flexibility to meet the needs of both participants and plan sponsors. Retirement income decisions are often personal and complex, particularly in the early years of retirement. Retirement income solutions should recognize this diversity of participant needs and address the practical requirements of plan sponsors. And three, the default solutions in defined contribution plans have proven effective in changing investment behavior. However, the stakes for a lifetime income default are quite high. Any proposed default lifetime income solution therefore avoid placing participants into a situation where they could permanently lose control of their retirement assets without having made an explicit decision. Any such default must recognize the legitimate preferences that some participants have for maintaining access and control over their retirement assets, particularly in the early years of retirement.

So, my first point is that defined contribution plan sponsors must play a major role in helping participants generate lifetime income. Why? Aside from social security, defined contribution plans represent the largest source of potential retirement income for millions of American workers. Unfortunately, most plan participants are largely uninformed about how to efficiently turn these assets into retirement income. Our belief is that the vast majority of Americans have a chance -- to have a chance at retirement -- secure retirement -- defined contribution plans must facilitate the ability to turn plan assets into income. Without as strong commitment by sponsors to help participants with these decisions, the 401k system will fail in its central mission to provide retirement security for American workers.

Retirement income is an area where participants are less informed and the problem is far more complex than in the accumulation phase. It is hard enough for most employees to figure out how to save and invest in the years before retirement. It is even more difficult to know how to invest and draw down your assets so that you do not run out of money. Unfortunately the typical 401k today does little

to facilitate participants getting the retirement income help they need, and this situation needs to change. Outside of the 401k system, most participants have no place to turn for high quality objective help and advice. The truth is that most participants are ignored by the financial services industry due to their relatively small investable assets. Participants with less than \$50,000 in their accounts are largely ignored by advisors while financial service firms vigorously hunt the smaller number of wealthy participants.

The scale economies of defined contribution plans make it possible for all participants to benefit from institutionally priced products and services that would otherwise not be accessible to them. Moreover, the fiduciary role that plan sponsors play in making sure that participants are protected is very important. Given the unfamiliarity of lifetime income products to plan participants, it is important that plan sponsors select and monitor appropriate solutions for their employees. Regulators and legislators need to provide clear guidance to plan sponsors as to how to satisfy their obligation to prudently monitor and select lifetime income solutions. The government should ensure that plan sponsors do not face unacceptable risks in helping participants with these critical decisions. But without the availability of effective lifetime income solutions within defined contribution plans, the 401k system will fail to deliver retirement security.

My second point is that the workable retirement income solutions in defined contribution plans require a substantial flexibility. The needs of retiring participants vary widely. Unlike the relative uniform requirements of younger employees, near retirees have substantial variation in their financial circumstances and preferences. For example, some participants may have other sources of retirement income -- for instance, a defined benefit plan -- while others do not. Some may have working spouses while others do not. Some are in good health. Others may suffer from chronic conditions. All of these differences can have profound impacts on the preferences for retirement income for a given participant. In our participant research, we have found that participants seek certain key features in any lifetime income solution: number one, the ability to receive stable income payments that won't run out in retirement; number two, income

payments that are protected from poor market performance both before and during retirement; and number three, the ability to maintain access and control over their assets. This last point -- maintaining control -- is especially important to retirees.

Evidence for these preferences is amply demonstrated by the overwhelming uptake of lump sum distributions for participants in both defined benefit and defined contribution plans. Today, in most situations, when given the choice between maintaining control over their assets or receiving lifetime income, participants overwhelmingly choose control. This behavior occurs even when the lump sum value of the benefit is demonstrably less than the lifetime income value being offered.

To be successful in defined contribution plans, lifetime income options must allow participants to maintain control of their retirement assets while still providing income. Participants do not want to be locked into a decision that they cannot change, particularly in the early years of retirement when uncertainty is at its greatest. The decision of how to employ insurance against longevity risk is not so much a question of if but of when. For many retirees, it will make economic sense to delay annuitizing their retirements until later in retirement. For some participants it will make sense to avoid annuitization all together. Plan sponsors also require significant flexibility in order to offer solutions in their plans. Retirement income solutions should be operationally easy to add to the plan. they must also be easy for sponsors to remove if they decide that their participants would be better served by a new solution in the future. Products that lock participants into irrevocable decisions can create problems for sponsors who may find it difficult to switch vendors or products that they decide are no longer in their participants' best interest.

My final point is that while default solutions have proven to be effective in changing in participant outcomes, the stakes for a default lifetime income solution are very high. Any proposed default lifetime income solution must avoid placing participants into a position where they could permanently lose access to their money without having made an explicit choice to do so. As we've seen with the success of the automatic enrollment initiatives and the use of qualified default investment alternatives, influencing

participants with a well-designed nudge to encourage better decisions through plan defaults is an effective strategy. However, the stakes for lifetime income decisions, particularly when it applies to annuitization are much higher than earlier in the accumulation phase. Losing control of one's assets in an irremovable way is a significant life choice for both retirees and, in some cases, for close family members as well.

Annuities are an important tool for managing this longevity risk but immediate annuitization at the point of retirement offers a dubious combination of inflexibility, unfamiliarity to participants and low or even negative economic urgency. In most situations, it will be beneficial for participants to delay the annuitization decision to a time when they are older. Setting up plan defaults where such annuitization decisions occur at retirement and are made for participants without their explicit consent could be hazardous. At best, such default strategies would yield sub optimal lifetime income decisions for many participants and at worst, a participant could wake up one day to discover that they no longer have control of their retirement assets. While the concept of a lifetime income default is sound, we strongly recommend that any default solution require a proactive participant decision before assets are irrevocably converted into lifetime income.

In conclusion, the 401k system to date has been solely designed as an accumulation vehicle. As the first baby boomers reach retirement age next year, we need to evolve the defined contribution system so that we can provide viable lifetime income for participants. We need to encourage plan sponsors to provide effective solutions to help participants receive retirement security. We look forward to continuing discussions with policymakers in the industry on this important issue, and we once again thank you for the opportunity to provide testimony.

Male Speaker:

Well, I may as well start. Mr. Hess you said, I think, since 2002 your company has provided benefits statements that show account balances in streams. And just out of curiosity, how frequently is that information disclosed -- do you disclose that information to your workers? On a quarterly basis? Annually?

Donn Hess:

Actually, more often than that. So, from a statement perspective, it's disclosed quarterly. It's also on the homepage of our website so anytime a participant were to authenticate and see the homepage, the number is disclosed there as well. Should somebody call in, our phone representatives can discuss it and then on some of our outbound targeted communications, specifically those focused on people who are saving below a six percent rate, that number is displayed in that communication as well.

Male Speaker:

Okay and subsequently I think you said that, that any regulatory mandate of a disclosure of this sort that would include projections should be accompanied by -- must be, I think you said -- accompanied by fiduciary relief of some sort in the event that participants believe that the projections are guarantees. And I guess I have sort of two -- one reaction and one thought to that. The reaction is, is it absolutely necessary, given that your company has been doing it since 2002 without a safe harbor of that sort, a relief of that sort, and B, can you sort of frame the contours of what you think would be an appropriate flavor of relief. I mean, what would it look like?

Donn Hess:

I think to answer the second part first, I think what Mr. Doyle described to the previous panel was exactly the kind of thing that we're thinking about. So, relief that encourages plan sponsors to share some level of projection at a basic construct but allows the flexibility to add detail. So generally, our stance is that any sort of projection is compelling to encourage positive behavior. The more specific you can make that projection, the more compelling it is. So we need that minimum level of relief to make that something that's comfortable in the plan sponsor community but to be wary that the ceiling prevents making that information as compelling as it possibly could be.

To the former, in terms of it absolutely must be provided, today we provide that number with a series of disclosures. Certainly that is something we could continue in the future. But guidance on what those disclosures should look like to make sure that we are in agreement in terms of how we're representing that number, that's helpful.

Male Speaker:
Thanks.

Female Speaker:
Actually, I do. I think it was one of you said -- I think one of you said that even -- that people choose lump sums even when the annuity is more valuable. Is that --?

Christopher Jones:
Yes, I made that comment.

Female Speaker:
And, of course, that's -- I didn't know -- I mean, I didn't know if you meant in a defined benefit plan context? I wasn't --

Christopher Jones:
Well, it -- generally in context where, if you were to look at the circumstances of that individual and sort of estimate the value of that annuity stream versus what they would get in a lump sum, people show a preference for lump sums.

Male Speaker:
I think maybe both of you expressed some skepticism or arguments against people kind of buying deferred annuities early in their careers and suggested that it might make more sense for lots of folks, or all folks, or many folks to wait for a later point in their career to purchase an annuity. I guess explain a little more about that and kind of what the -- I would assume there are other -- that the price of the deferred annuity would be low at a lower, you know, at an earlier point in retirement so that they're countervailing arguments, but if you could talk a bit more about, you know, what the arguments in favor of kind of the early purchase of deferred annuities versus waiting until later might be --

Christopher Jones:
So I can maybe take the first crack. I'm sure Donn has thoughts as well. The issue with respect of when to annuitize is an interesting one. Certainly there is -- if you make the issue binary, whether to annuitize or not, there's clear economic value to protecting against longevity risk, and that value obviously goes to the participant. When talking about the question of when to

annuitize, though, however, the issue of when has a big impact on the value of that annuitization.

When you purchase an annuity -- let's just take a very simple case where you're purchasing a fixed annuity at retirement -- you're purchasing a portfolio of different kinds of insurance. Some of that insurance is protecting you against those outcomes that are very valuable to protect against; that is, when you live to be 90 or 100 or 105 years old. But you're also buying insurance for outcomes that are very, very likely; that is, next year, you're very likely to be around and you're buying insurance that you're going to get a payment next year. The value of that insurance is different in different time periods. For most of these deferred annuity types of products it had been marketed in the 401k space, they are substantially more expensive than similar fixed income options that perhaps could provide, for instance, those income payments in the early years of retirement when you're almost certainly going to be around to collect them, and therefore, you would be better off to delaying that annuitization decision to some point later in your retirement years. And so if you look at it from an economic efficiency standpoint, there are strong reasons to defer that annuity decision for many participants.

Overlaid with that is a very strong behavioral bias that people have for wanting to have control and flexibility early in their retirement years when uncertainty is high. And so for both of those reasons we don't believe -- there are some countervailing reasons why you might want to introduce those products for earlier folks, certainly the behavioral impact of slowly translating your balances into an annuity stream. You do get the benefit of locking in the mortality curve, if you will, in the future which has some value. But we do believe, overall, at least based on the kinds of products that are in the market today that you would be better off deferring that annuitization in many situations.

Donn Hess:

So I think looking at the product set that exists today, we would agree with Chris's assessment. Some of the testimony prior to -- to our testimony talked about where we would anticipate the market was going, and I think with that anticipation in mind we would still err on the side of any legislation allowing a certain amount of variability and

that comes into plan design changes. So when you look at offering annuities to a younger population and you assume that we have solved some of the pricing issues that Chris describes, you still have a lot of variation in industry types. So that type of solution could make a lot of sense for a plan sponsor that administers a plan where the 401k is the primary accumulation vehicle for assets and there's very little turn over in that population so they have the ability to accumulate assets over time and build that annuity up in some meaningful way. If, however, you're looking at a sponsor that sees quite a bit of turnover, has multiple plan types, then mandating or even encouraging that particular product set doesn't make as much sense even should we solve the pricing issues that Chris described.

Male Speaker:

I have a question for Mr. Jones. As you think about your client base, can you talk about just any changes you've seen in the demographics of the adoption of annuities? Have you seen an uptick? Has it been fairly stable? Then across your clients, do you see certain design features that tend to have a more positive impact with respect to higher adoption rates?

Christopher Jones:

So our client base is overwhelmingly formed from large employers. Our average clients are on the order of a billion dollars in plan assets. In that client base today we don't see -- I believe this is true -- any single client that has a deferred annuity or some type of annuity in plan solution that they're offering today. We do have a number of clients that are providing the ability for participants to purchase institutionally priced annuities at the point of retirement when they get out of the plan. There, typically the adoption rates are in the very low single digits. We've not aware of any plan sponsor that has figured out how to get those adoption rates up. Some of our sponsors even allow people to purchase, in effect, take their money and put it in the DB plan and purchase the DB income. Even in those circumstances, the numbers of people they're able to get to do that are very, very small. I do think that offering partial annuitization could be helpful in that regard and not many employers allow this yet but to the extent that that was more widely available I think that would help the circumstances.

I think we are always going to be facing a very, very powerful behavioral bias that people have of wanting to maintain control of those assets, particularly at the point of retirement. This is a point in time when people are under a lot of stress. There's a lot of uncertainty about what their future lifestyle will be like. They have perhaps even concerns about how long -- you know, what their longevity will be. All of those circumstances make it very difficult to make that irrevocable decision to take balance and turn that into income even if there's a lot of benefit to doing so.

Robert Doyle:
Any other questions?

Male Speaker:
Maybe just one. I think I understand the rationales for why many participants would want to defer a decision about purchasing an annuity and why it might be beneficial for many to defer the decision, but there is a flip side to that that maybe we haven't talked about as much, and that has to do with the selection and pricing of the annuities associated with that. That if people are deciding to accumulate an annuity during their accumulation phase or if they're buying a longevity insurance style deferred annuity, that buying that at the point of retirement rather than when they actually turn 80 years old, they're in a different risk pool, so presumably they'd get a better price. Can you just react to that and how that contrasts that with the other point?

Christopher Jones:
Yes, I think both your points are accurate. If you're purchasing the annuities earlier in your lifetime, you are generally going to be part of a risk pool that is different than people that are purchasing later in life. I think the most economically efficient way to annuitize is to deal with -- essentially use these longevity insurance contracts. So if you're pre-committing to annuitization in the future then you're going to get the maximum bang for your buck in terms of the benefit of that longevity insurance versus the cost to you of that longevity insurance. We strongly agree with I think one of the panelists on the previous panel for MetLife that the required minimum distribution rules for longevity insurance should be changed because right now they're prohibiting the use of those types of products within 401ks, and that's

clearly something that's not in the best interest of participants.

The challenge here, though, again gets to a key question of cost. So you have to look at not just at the assumptions being used to price the annuity in the pool of applicant, but you also have to look at what are the costs being built into the products themselves. By and large today, the costs of those products are quite substantial and exceed the cost of similar types of fixed income solutions by substantial margins at least in the large plan market. So even if you're giving up a little bit as you're going to have to pay a little bit more because you're going to be part of an applicant pool that is going to be on the balance, healthier, we still think it can make substantial sense to defer that decision at least by some number of years early in retirement.

Male Speaker:
Thanks so much.

Robert Doyle:
Okay, if there are no other questions, we thank you for your participation. We thank all the panelists who participated in today's hearing and we're looking forward to starting again tomorrow at 9:00.

[end of transcript]

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