



RESPONSE OF:

ALLIANZ LIFE INSURANCE COMPANY OF NORTH AMERICA

AND

ALLIANZ LIFE INSURANCE COMPANY OF NEW YORK

To:

DEPARTMENT OF THE TREASURY

AND

DEPARTMENT OF LABOR

**INFORMATION REGARDING
LIFETIME INCOME OPTIONS FOR PARTICIPANTS
AND BENEFICIARIES IN RETIREMENT PLANS**

DATED: SEPTEMBER 9, 2010



INTRODUCTION

Allianz Life Insurance Company of North America, established in 1896, and its New York-based affiliate, Allianz Life Insurance Company of New York (collectively, “Allianz”) submit for consideration by the Department of The Treasury and the Department of Labor (the “Agencies”) its response to the August 6, 2010, Response to Certain Issues Relating to Lifetime Income Options for Participants and Beneficiaries in Retirement Plans (“Response to Certain Issues”).

Allianz thanks the Agencies for their inquiry into this important issue. Hard-working U.S. employees nearing retirement require education and options to ensure a secure future. Defined contribution participants should have open and informed access to financial products that protect against market volatility and longevity risk – both during accumulation of their retirement funds and during distribution (“income”) from those funds.

Allianz believes that plan participants (a) need access to education and guidance on retirement planning; (b) need the ability to purchase secure retirement products with principal guarantees; and (c) need to be able to easily convert a portion of their accumulated retirement assets into guaranteed lifetime income.

Allianz encourages defined contribution plans to make enhanced educational materials available. These materials should educate consumers about the value of properly designed lifetime income solutions during the accumulation and income phases. Plan sponsors should also be encouraged to provide face-to-face guidance from a variety of financial professionals. We recommend permitting and encouraging in-plan and out-of-plan solutions, which will require reconciling complex tax laws and incentives. Allianz recommends avoiding a generic default option, and further recommends that the educational requirement include both in-plan and out-of-plan (“roll over”) solutions.

In a recently conducted consumer study^{*}, Allianz learned that Americans aged 44-75 believe there is a retirement crisis (92 percent) in the United States. Although 61 percent fear outliving their money more than death, nearly one-third (31 percent) say they are not clear about what their expenses will be in retirement, and 36 percent have no idea if their income will last. When asked how much yearly income is needed in retirement, respondents indicated a median income of \$59,000 per year. Unfortunately, respondents were off by a factor of nearly three times when estimating how much they’d need to save to create that household income.

^{*} Larson Research and Strategy Consulting, Inc. and DSS Research fielded a nationwide online survey for Allianz among 3,257 U.S. adults, age 44 to 75. The margin of error for the total sample was approximately +/- 1.7%. The online survey was conducted in the United States between May 6th, 2010 and May 12th, 2010. In addition to a representative sample of 1,642 US households, sub-samples of more affluent households and households who own annuities were also targeted. Results were weighted by age, gender, education, race/ethnicity and income to account for disproportionate sampling of certain populations.



Allianz is uniquely positioned to provide insight with respect to lifetime income options and to respond to the Response to Certain Issues because of its more than 20-year history of developing innovative annuity products that encourage individuals to receive guaranteed lifetime income rather than lump sum payments. Allianz currently insures more than one million annuity contract holders and manages account values in excess of \$72 billion.

Allianz Life provides life insurance, and fixed and variable annuities in the United States as a subsidiary of Munich-based Allianz SE, a global financial services group, which employs nearly 155,000 people worldwide with approximately 75 million customers in 70 countries and €926 billion of third-party assets under management (as of December 31, 2009). Other North American affiliates of Allianz SE include the property and casualty insurance company Fireman's Fund, and Allianz Global Investors, a network of mutual fund, hedge fund, and asset management companies that includes the subsidiaries PIMCO, Nicholas-Applegate Capital Management and Oppenheimer Capital.



1. Certain specific participant concerns affecting the choice of lifetime income relative to other options (e.g. long-term viability of product providers, inflation risk, fees, complexity and lack of death benefits and withdrawal options)

Insurers are regulated and rated to assure financial strength and solvency

Life insurers are among the most highly regulated and rated entities in the financial services industry. As consumers contemplate their financial options, they need to be assured by regulators that the industry generally has a long track record of financial strength and stability.

As an example, Allianz Life and parent company Allianz SE have received some of the highest financial strength ratings available from Standard & Poor's, A.M. Best and Moody's. Below are current ratings:

- Standard & Poors – Allianz Life – AA (very strong); Allianz SE – AA (very strong)
- A.M. Best – Allianz Life – A (excellent); Allianz SE – A+ (superior)
- Moody's – Allianz Life – A2 (Good); Allianz SE – Aa3 (Excellent)

These independent agencies conduct an annual analysis of financial results and evaluate management objectives and strategies. They review capital adequacy, product diversification and numerous other factors bearing on the long-term strength of the company. Moreover, Allianz Life retains the financial backing of one of the largest financial enterprises in the world in Allianz SE. During both the Great Depression and the economic crisis of 2008-2009, Allianz Life met all of its claims-paying obligations to customers.

Allianz and other firms are innovating and designing products that address inflation risk, interest rate risk and other market risks

Allianz offers consumers a number of fixed index, fixed and variable annuities. Our fixed index and fixed annuity products are designed to help our clients reach their retirement goals. They offer tax deferral, the opportunity for guaranteed interest or market indexed growth and the protection of guaranteed lifetime income. Allianz also offers variable annuities that provide a variety of income and death benefits designed to help meet our clients' financial goals and retirement needs. Our variable annuities provide market participation along with benefits that help provide a level of protection for their investment and their beneficiaries.

Fixed annuities are long-term products built for protection, during both accumulation and income distribution phases, which reduces the effect of volatility. And variable annuities, through various guaranteed benefit riders, can also offer levels of protection during accumulation and/or income distribution. In selecting among these products, purchasers are inherently making trade-offs between liquidity and growth potential.



Inflation risk will continue to be a concern that retirees and pre-retirees must consider in their retirement planning. Allianz' *Reclaiming the Future* study indicated that more than 70 percent of pre-retirees consider inflation/tax increases to be extremely important when planning for retirement. At an inflation rate of 3 percent compounded over 20 years, a level retirement income is estimated to lose nearly half of its purchasing power. Allianz has a history of developing products that address these concerns, including our annual payment increase feature and inflation-oriented solutions.

Annuity products are also designed to address other market risks, specifically volatility. In the case of defined contribution plans, the volatility risk is not fully understood by consumers and can have a significant effect on the lump sum that a participant has available to convert into a lifetime income stream. An annuity has the ability to guard against a portion of the volatility risk inherent in market participation, while still providing opportunity for growth potential. Essentially, an annuity protects against downside risk while offering upside potential, something that today's plan participants need to have as an option for their retirement.

Annuities are becoming increasingly flexible and offer multiple withdrawal options

Annuity products continue to evolve and offer increased flexibility for consumers. Some of the newer generations of products utilize more of an "a la carte" approach and/or allow consumers to attach riders with certain benefits, specifically lifetime income riders. Most annuities allow the contract owner to withdraw a limited portion of the value of the annuity, such as 10 percent, each year free of any surrender charge. Many annuities also include additional liquidity options in the event of death, or if the purchaser enters a nursing or assisted living facility. Further, modern annuity design has made significant strides in providing for flexible asset payout streams.

Because Allianz is the leading provider of fixed index annuities, we will be focusing our comments on this product solution.

Product design should provide options to consumers – options should not be reduced for simplicity alone as consumers need the benefits these options provide

Consumers tell us that they want choices; different benefits are a fit for different individuals based on a wide variety of personal needs. Individuals currently have access to many different variations of annuities that provide guaranteed lifetime income. There are those designed to be used with other investment options outside the annuity itself. There are options designed for future guaranteed retirement income, allowing consumers to have guaranteed growth in their income guarantee while they have not started income distribution. Some provide greater benefits the longer the consumer waits to take income distribution, but do not make deferral mandatory. This level of choice in annuity products is important because it allows the product to be flexible to change with the client through their various life stages.



Old perceptions and myths linger on annuities

Allianz recently investigated Americans' perceptions of annuities and found that old views and myths still linger about the products. The Allianz *Reclaiming the Future* study, which surveyed 3,200 Americans aged 44-75 in May 2010, found that 54 percent of people surveyed express distaste for the word annuity – even after describing an annuity-like product as their ideal financial vehicle. Meanwhile, an overwhelming 80 percent preferred a hypothetical product with four percent return and a guarantee against losing value over a hypothetical product with an eight percent return and subject to market risk. These survey results demonstrate the need for education about annuities and their place in retirement planning.

Much of this bias is based on legacy information that is decades old. Fifty-three percent first formed their opinion of annuities 10-20 or more years ago, and 64 percent of those respondents haven't researched annuities since that time. Thus, many myths and misconceptions continue to plague these products today. In fact, only 27 percent knew of innovations made with annuities during the past 5-10 years, and even fewer (23 percent) realize that variable annuities allow contract holders to participate in market gains.

Our research has shown that when people understand annuities, they're extremely satisfied with them. According to the study, 76 percent of annuity owners are "very happy" with their purchase. More than half of owners like the product because it's a safe, long-term investment vehicle (57 percent), a great way to supplement their retirement income (56 percent), and an effective tool to get tax-deferred growth potential (56 percent). In fact, consumers ranked annuities second-highest (50 percent) in satisfaction among all financial instruments, beating out mutual funds at 38 percent, stocks at 36 percent, U.S. savings bonds at 35 percent and CDs at 25 percent.

This survey also showed that more Americans are now seeking safety and guarantees over growth. When asked what features they find most important in a financial product, the top feature was "the ability to create a stable, predictable standard of living throughout retirement" followed by the "ability to provide a guaranteed income stream for life." Similarly, when asked to choose between putting money into an annuity-like solution (moderate growth opportunity, monthly income, but limited access to the lump sum) versus a similar instrument that provides total access but risks running out of money, 56 percent chose the annuity-like solution.

These results demonstrate that more education is needed about annuities because perceptions need to change if consumers are to access guaranteed income and create a more stable retirement. The 401(k) industry successfully educated consumers about mutual funds to save for retirement; now government and the industry need the same type of concerted education effort on annuities and how they can help Americans when they are in retirement.

The industry must do a better job of simplifying product language

As the Allianz survey results show, consumers are eager to learn more about the benefits that annuities can provide. By simplifying some of the terminology, regulators and the industry can



help to make the products better understood and accepted by mainstream consumers. In addition, because people's opinions of annuities were formed 10-20 years ago, myths about annuities need to be dispelled and annuity innovations explained to better showcase the ease with which annuities can help consumers to meet their retirement needs.

2. Information useful to making choices on spending down retirement

Various income options provide flexibility to meet consumers' needs in retirement through either scheduled payments, payments that last your lifetime or a lump sum. Defined contribution plans have long held an accumulation-oriented focus on planning and advice. Because of this, there has also traditionally been a bias against the very products (annuities) that can best address longevity and volatility risk, which are two of the most important risks participants will face in spending down in retirement.

Traditional defined contribution plan participants have access to an abundance of well-meaning but often misguided information about how to plan for income in retirement. These materials often compare annuities with investment products on the basis of rate of return (growth potential), and do not sufficiently address the risks associated with longevity or mortality. In addition, these materials often fail to adequately describe the features and benefits of both in-plan and out-of-plan annuities. Inadequate information is one of the root causes for individuals failing to adequately and appropriately plan for income needs in retirement.

Annuities and lifetime income products are often mistakenly compared to "equity investments." This comparison is not appropriate as each serve different purposes. Annuities are designed to minimize volatility by providing guarantees;¹ equity investments are designed to maximize growth potential and liquidity. Researchers have, in fact, observed that because retirement income products such as fixed index annuities "have not been designed to compete with equity mutual funds or exchange traded funds," it would be improper to compare one against the other.²

More education is needed for participants to truly understand longevity risk and the tradeoffs between liquidity, growth and protection. There remains a tension between consumer objectives of full liquidity (i.e. full control over the account value) and structured product income guarantees (which typically offer reduced or no control over account value). Experience shows that consumers regularly choose liquidity over income, which is often not the most appropriate choice in their circumstances. Liquidity can be costly both in terms of financial resources for long periods of time and in unintentionally allowing participants access to funds

¹ Research published in the fall of 2009 indicates that for the five-year period from 2003 – 2008, the S&P 500 average return was 3.18%, where representative fixed index annuity return for the same period was 6.05%. This shows the value of product guarantees and floors in a rapidly declining market. Marrion J., VanderPal G., Babbal D., *Real World Indexed Annuity Returns*, Wharton Financial Institutions Center, October 5, 2009.

² *Id.*



that they may spend down faster than is prudent. Once consumers receive education and then understand the tradeoffs, the guaranteed income option becomes more attractive.

Allianz recommends participants work with a trusted financial professional in an open format and not limited to a small number of professionals selected by their employer.

Individuals should be provided access to many different variations of annuities which provide lifetime income guarantees. In the general market, consumers have the opportunity to make their annuity selection based on the three factors of volatility, liquidity and growth potential. In most cases, they have financial professionals who help them to make informed choices about which annuity is best for their individual circumstances. Judging by their annuity choices, consumers have clearly voted in favor of a *balance* of growth potential with liquidity and a level of guaranteed income versus a pure income guarantee.

A small number of defined contribution plans offer annuities, and most have very low election rates. Allianz believes this may stem from participants' lack of understanding of the balance that must be struck among the three factors of volatility, liquidity and growth potential. It is likely that, similar to the individual market, the guidance of well-informed financial professionals can make the difference. At the very least, there needs to be education in a format that helps plan participants understand their own priorities when it comes to providing for their retirement financial needs. Plan sponsors can play an important role in assisting participants by not only offering annuity options, but also by giving them access to trusted financial professionals who can help them make informed choices. It is also important that sponsors create open formats and not limit the number of professionals to a small number selected only by the employer. Participants need to have access to professional options that are appropriate to their own financial circumstances as they seek guidance.

Annuities are not the entire solution but should be a part of a well-balanced portfolio, giving participants a baseline of protected assets and guaranteed income.

To be clear, Allianz does not believe that annuities are the entire solution for participants. Instead, they should be considered as a part of a well-balanced portfolio. In many ways, the annuity offers the baseline of consistent, secure and guaranteed income on which a participant can rely throughout employment and then retirement. It may be completely appropriate for participants, based on the advice of a trusted financial professional, to continue to hold a portion of their assets in stocks, bonds, mutual funds and other investment options in retirement. However, given the critical nature of retirement planning, and the relative lack of financial sophistication of many employees, it is essential that participants apply a significant portion of their retirement money to products with principal and payout guarantees.

Allianz survey results suggest consumers need and want help

According to the Allianz study *Reclaiming the Future* referenced above, three-quarters of respondents currently work with or are receptive to working with a financial professional. This suggests that people are eager to take a more active role in their planning to ensure they have adequate retirement income for the future. Even more encouraging, consumers are now



focusing more on protection of their retirement assets rather than purely growth investing goals such as high rate of return.

Allianz recommends increasing education on options

Planning in defined contribution plans often tends to focus primarily on accumulation versus income strategies. As they plan for retirement, participants need to understand how to build their defined-contribution assets, and then efficiently convert a portion of those assets into a guaranteed stream of lifetime income. To bridge the gap between the accumulation and guaranteed income phases of retirement planning, participants need effective education about the risks they will face while employed and when in retirement. They also need products that are designed to specifically provide longevity risk protection. Annuities should fulfill the core position in such financial planning approaches. By design, annuities are insurance products that can guarantee a lifetime stream of retirement income. Annuities are the only product that can provide this guarantee.

3. Value of lifetime stream of income vs. a lump sum distribution (specific questions about structure of benefits, how they are depicted on statements, contribution rates, rates of return, interest rates used for conversion, mortality rates, actuarial equivalents of an account balance in form of lifetime monthly benefit, computer models and costs)

A problem for plan sponsors is that the typical participant is not sufficiently financially sophisticated to understand the implications of taking a lump sum and then personally managing the money in a drawdown that may last 20-30 years. The reason annuities are useful is that they help provide an income stream that is based on pooled risk (something only life insurers are able to do) whereas a lump sum simply cannot pool risk. Participants need to be educated so they can understand what pooling of risk means when investing assets through a life insurer, which has the ability to protect against loss of principal and provide guaranteed income for life.

Income streams can be paid to an employee even after incapacitation; lump sum means an employee's assets might not be managed after incapacitation

The Agencies need to consider that representations made during plan enrollment and at distribution, which may sway a participant's decision-making, are only a snapshot at a certain point in time. As people age, the ability for a consumer to make wise personal financial choices diminishes. It is often the case that a consumer does not fully appreciate or anticipate their own future inability to make good choices for themselves (or their spouses) due to physical incapacitation. Therefore, a choice to take a lump sum payment at the age of 65, with a belief one can manage his or her money effectively at age 85 or 90, factors into the type of offerings a plan should provide. Plan sponsors need to understand and anticipate the potential over-confidence young retirees may have in their long-term ability to manage their lump sum. An annuity-based solution for a portion of one's portfolio takes away some of the risk of mismanagement of assets due to incapacitation.



Plan sponsor, trade associations and educational institutions can play a role to support direct-to-consumer education

Plan sponsors have been successful in their education efforts around appropriate accumulation behaviors inside a defined contribution plan. Their new imperative will be to educate participants about the importance of lifetime streams of income, longevity risk and the dangers that incapacitation may have on one's ability to manage down assets in retirement. Employees need to have institutions protecting their interests and giving them broad guidance. Plan sponsors can play a role, with cooperation from financial services trade organizations and educational institutions, to help plan participants make the best decisions for themselves as they enter retirement.

4. Fiduciary safe harbor for selection of lifetime income issuer or product

Plan sponsors and professionals to DC plans should have safe harbor provisions extended for use of annuities both in-plan and out-of-plan. Insurers are highly regulated and well capitalized. Lifetime income is an important part of retirement planning, and insurers are best suited to pool risk and provide guaranteed solutions for plan participants. Plan sponsors and professionals should have the ability to offer – and feel safe about offering – annuity options because they are the only product that can provide guaranteed income for life.

Education is the best tool to assure participants understand their options and appropriately dedicate a portion of their savings to annuities as a part of their retirement planning. Allianz is prepared to assist regulators, consumers and plan sponsors with determining the best options to support asset protection and guaranteed income for life for plan participants.

5. Alternative designs of in-plan and distribution lifetime income options

As mentioned above, annuities should be an option in-plan and at distribution as a roll-over option. At roll-over, a good plan would set up a variety of annuity options from multiple annuity issuers so participants have choice. At least two to three annuity issuers are required because all annuities are not alike.

Allianz recommends that the Agencies consider adopting rules that encourage defined contribution plans to make enhanced educational materials available. These materials should educate consumers about the value of properly designed lifetime income solutions during the accumulation and distribution phase. Plan sponsors should also be encouraged to provide face-to-face guidance from a variety of financial professionals. The rules should permit and encourage in-plan and out-of-plan solutions. Doing so requires reconciling complex tax laws and incentive schemes. However, Allianz recommends avoiding a generic annuity option, and we further recommend that the educational requirement include both in-plan and out-of-plan (“roll over”) solutions.

Out-of-plan options do not require a plan sponsor to select a single annuity provider, nor do they limit participants' choices to the products offered by a single annuity provider. They also allow individuals to receive individualized education and facilitate the recommendation and



selection of an annuity based on the participant's individual financial situation and retirement income needs. Out-of-plan annuities are portable because the benefits stay with the employee when the employee changes jobs or when plan sponsors move to a different administration platform. They are, in effect, an open-architecture selection opportunity for consumers, allowing individuals to choose the annuity provider and annuity product that meet their needs.

Allianz believes that plan participants need access to education and guidance on retirement planning and need to be able to easily convert a portion of their accumulated retirement assets into guaranteed lifetime income.

Conclusion

Employees who have worked hard and have planned for retirement should not be abandoned at the point of retirement by a financial culture that has chosen to over-emphasize retirement accumulation to the virtual exclusion of retirement income planning. Defined contribution participants should have open and informed access to financial products that protect against market volatility and longevity risk – both when they are accumulating their retirement funds and at any point when they are taking distributions from those funds. Allianz believes it is critical that participants in defined contribution plans be educated about receiving plan distributions in the form of an income stream, rather than solely as a lump sum distribution. Plan participants should not be in a position where living a long life is undesirable.

Working with the financial services industry and consumer advocacy groups, the Agencies should create a mandatory list of financial principles, written in everyday language, to which every plan participant must have access at all times during their participation in the plan. This mandated list should include principles to help the consumer understand how to accumulate as well as convert their accumulated benefits into some form of guaranteed lifetime income.

Allianz also believes that consumers should have access to a wide variety of annuities in order to have the opportunity to select an option based on their individual needs. Allianz submits that the option of selecting an out-of-plan annuity provides investors with access to a wider choice of options and other benefits not currently available with in-plan options. Therefore, Allianz submits that the Agencies should avoid making policy decisions that could have the effect of limiting access to consumer choice among insurance providers and guaranteed lifetime income solutions or favoring the use of in-plan options to the detriment of out-of plan options.

Allianz is prepared to assist regulators, consumers and plan sponsors with determining the best options to support asset protection and guaranteed income for life for plan participants.

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