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

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

RIN 1210-AB33

DATED: MAY 3, 2010

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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 February 2, 2010, Request For Information Regarding Lifetime Income Options for Participants and Beneficiaries in Retirement Plans (the "Lifetime Income RFI").[1] Allianz is uniquely positioned to provide its insight with respect to lifetime income options and to respond to the various questions raised in the Lifetime Income RFI because of its 20-year history of designing annuity products that encourage individuals to receive guaranteed lifetime income rather than lump sum payments. Allianz currently insures more than one million annuity contractholders who, as of March 31, 2010, had a combined contract value in excess of $72 Billion.

Allianz provides life insurance, and fixed and variable annuities in the U.S. Allianz Life Insurance Company of North America and Allianz Life Insurance Company of New York are subsidiaries 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.

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.

In addition to this response, the Agencies have received a response from Allianz of America, part of Allianz SE and an affiliate of Allianz Life Insurance Company of North America, which considers some behavioral finance issues that are important for the Agencies to consider.

EXECUTIVE SUMMARY

Allianz expects that the Agencies will receive responses to this Lifetime Income RFI that will provide wide-ranging, comprehensive and question-by-question answers to the issues the Agencies have raised.[2] In this response, Allianz will focus on some often overlooked, yet essential, concepts Americans must understand to better plan for their retirement needs.

When planning for retirement there are two phases: the accumulation phase and the distribution phase (otherwise referred to as the "income phase"). To effectively plan for and manage their retirement assets during both phases, individuals must understand and balance

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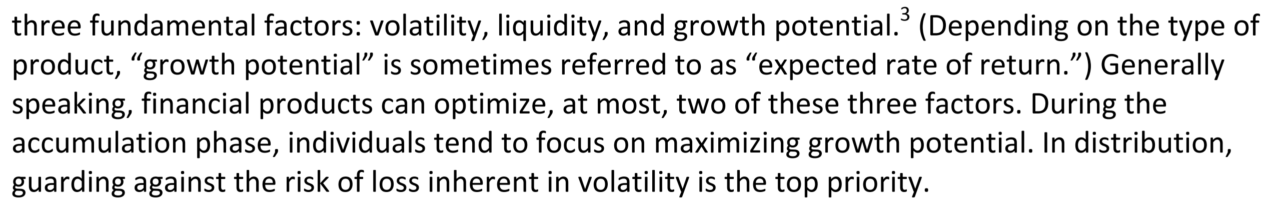
[1] Request for Information Regarding Lifetime Income Options for Participants and Beneficiaries in Retirement Plans, 75 Fed. Reg. 5253 (proposed February 2, 2010).

[2] In fact, two trade organizations to which Allianz is a member, the American Council of Life Insurers and the Insured Retirement Institute, have provided such responses and Allianz commends each to the Agencies' reading.



three fundamental factors: volatility, liquidity, and growth potential.[3] (Depending on the type of product, "growth potential" is sometimes referred to as "expected rate of return.") Generally speaking, financial products can optimize, at most, two of these three factors. During the accumulation phase, individuals tend to focus on maximizing growth potential. In distribution, guarding against the risk of loss inherent in volatility is the top priority.

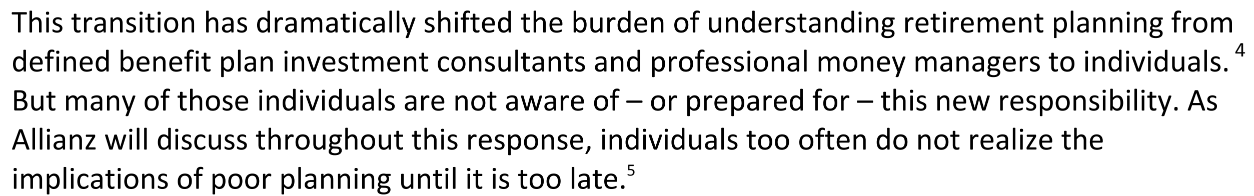
Current retirement planning, particularly in defined contribution plans, generally focuses almost exclusively on the accumulation of assets. As a result, plan participants are not able to place the appropriate focus on ensuring a guaranteed source of lifetime income. To bridge the gap between the accumulation and guaranteed income phases of retirement planning, participants need effective education about the risks they will face 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 in the market that can provide this guarantee because only insurers can pool risk.

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. Guaranteed income options allow consumers to individually balance the three factors of volatility, liquidity, and growth potential.

Americans are facing a dramatic shift in retirement planning as the sources of guaranteed lifetime income have changed. For decades, most Americans have had a reliable retirement safety net of Social Security benefits and employer defined benefit plans. Personal savings augmented these guaranteed sources of income. And for much of the past century, most Americans have planned for their retirement assuming that their Social Security and pension benefits would be guaranteed for as long as they lived. These two income sources were the cornerstones of a retiree's guaranteed lifetime income.

Under that model, the government and the individual's employer were essentially managing the individual's longevity risk. But over the past two decades, most American employers have replaced their pension plans with defined contribution plans, transferring to the employee full responsibility for a prudent savings plan and wise investment of those savings. Additionally, we know that – because an increasing number of Baby Boomers are retiring – many are questioning the ability of the U.S. Social Security system to continue to provide benefits at current levels and eligibility ages. These fiscal strains and retirement trends are further compounded by demographic trends: Americans are living longer and, therefore, expecting to dip into these plans for many more years than was originally anticipated.

[3] See Statement of Gary Bhojwani, *Advising Seniors About Their Money: Who Is Qualified and Who Is Not?*, Senate Special Committee on Aging, September 5, 2007.



This transition has dramatically shifted the burden of understanding retirement planning from defined benefit plan investment consultants and professional money managers to individuals.[4] But many of those individuals are not aware of – or prepared for – this new responsibility. As Allianz will discuss throughout this response, individuals too often do not realize the implications of poor planning until it is too late.[5]

Both plan sponsors and plan participants need to better understand this new reality and take action to address it. Allianz understands that bringing lifetime income solutions to defined contribution plan participants is not simple and, in this document, we will address some of the challenges that must be overcome to achieve this goal.

Therefore, 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 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 default option, and we further recommend that the educational requirement include both in-plan and out- of-plan ("roll over") solutions.

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

This response to the Lifetime Income RFI has four core sections.

- Section I, Allianz will examine how annuities can play a pivotal role in providing for lifetime income.
- Section II, Allianz will examine the challenges to the inclusion of annuities in defined contribution plans.
- Section III, Allianz will discuss some of the flaws in current retirement planning that can lead to consumer lack of interest or even adversity to guaranteed lifetime income solutions.

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[4] "[E]mployees are not only increasingly responsible for the adequacy of their savings at the time of retirement, but also for ensuring that their savings last throughout their retirement years [. . .] Lifetime Income RFI, 75 Fed. Reg. at 5254.

[5] See, Kessler, E. *Constructing New Retirement Systems*, Pension Research Council, August 2009. "Individuals are poor at retirement planning and make poor choices, the consequence of which (inadequate retirement wealth, outliving retirement assets) are not realized until the individual is older and poor outcomes may not be remedied easily." *Id*. at 2.

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- Section IV, Allianz will make specific recommendations to the Agencies.

I. Annuity Products Are Critical to Lifetime Income

Allianz recommends that the Agencies consider adopting Rules that both permit and affirmatively encourage annuity solutions as part of a comprehensive retirement program in defined contribution plans. This would help address the new reality that consumers need to rely more heavily on personal savings (a majority of which are often held in defined contribution plans) to adequately provide for their financial retirement needs. Where defined benefit plans had, in the past, provided consumers with guaranteed income solutions for retirement, plan participants now need to find their own ways to protect their retirement income needs based on their individual circumstances.

To plan for financial protection during their retirement, plan participants will need to understand and determine their individual priorities relating to volatility, liquidity and growth potential.[6] While this is a very basic premise in the financial industry, Allianz believes it is often overlooked by plan sponsors and individual retirees in selecting products. Active consideration of these factors may help increase consumer selection of guaranteed lifetime income options.

Fixed annuities are long term products built for protection, during both accumulation and income distribution phases, which reduces the effect of volatility.[7] 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.

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[6] Inherent in the questions in the Lifetime Income RFI, is the Agencies' understanding that plan participants may not act to protect themselves, absent adequate education and professional guidance. This is an important component that Allianz will address in Section III.

[7] Fixed annuities are annuities with guaranteed principal and minimum rates of return. The insurance company can declare and credit a higher rate of return. Indexed annuities are annuities with guaranteed principal. These annuities have indexed options that credit interest based on the performance of a public index (e.g. S&P 500 index), subject to a floor of zero. The interest crediting methodology typically will limit full participation in the gains in index performance, reflecting the cost of the guaranteed floor of zero.

Note in both product designs, charges may result in the purchaser receiving less than the amount paid for the annuity upon a full surrender.

A. During Accumulation

Fixed deferred annuities[8] provide guarantees on contract values.[9] The design is intended to protect consumers' nest eggs, especially during periods of market volatility. While there are a number of design variations, two basic frameworks of fixed deferred annuities are discussed below.

Guarantees can be provided in the form of guaranteed principal protection and a minimum rate of return. These guarantees reduce volatility but also the potential for asset growth in comparison to financial products that have a weaker guarantee or no guarantee at all.

Guarantees can also be provided in the form of a minimum contract value at a specified interval, e.g. on the tenth anniversary of the annuity. Fixed and variable annuities with this design offer individuals the ability to select one or more crediting formulas or different investment options available through the annuity. The crediting rate formulas or the investment options provide the potential for increased retirement asset growth.

In the context of annuities, liquidity is access to or control of the contract value. Assuming that a primary objective for purchasing an annuity is to minimize volatility (the risk of large reductions to principal), then consumers must be willing to trade off some liquidity and some potential for higher future retirement savings. Annuities generally contain many "insurance" features that permit contract owners to access a significant portion of their contract value in an emergency or for cash flow purposes without the imposition of any surrender charge.[10] For example, most annuities allow the contract owner to withdraw a limited portion of the value of the annuity, such as 10% each year free of any surrender penalty. Many annuities also include additional liquidity options in the event of death, or if the purchaser enters a nursing or assisted living facility. For qualified annuities, which require that the owner must withdraw I.R.S. required minimum distributions ("RMD") starting at age 70 ½, contracts often waive applicable surrender charges on such RMD payments.[11] All these liquidity features do have a cost that is reflected in a potentially lower growth potential of the annuity.

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[8] A deferred annuity is an annuity with guaranteed income options that can be accessed in the future.

[9] Contract value is the value accumulated within the annuity.

[10] As a long term financial product, annuities often assess surrender charges if the contractholder terminates an annuity prior to the end of the surrender period. Among other purposes, surrender charges, and certain other contract design parameters, tend to encourage persistency and thus permit insurers to invest in longer maturity, higher yielding bonds, which may permit the insurance company the ability to provide more generous non-guaranteed benefits to policyholders who use the annuity as intended. They also help the company recover some of the cost of the significant investment in the product, promote equity among persisting customers and non-persisting customers and protect solvency.

[11] Annuities also have multiple other payout options, ranging from periodic income options to full lump sum liquidity (which is often subject to contractual penalty).

B. During Distribution

Even more important in the context of providing longevity risk protection, there is a tension between consumer objectives of full liquidity (i.e. full control over the contract value) and structured product income guarantees (which typically offer reduced or no control over contract value). Experience shows that consumers regularly choose liquidity over income unless they understand the tradeoffs.

Liquidity can be costly. A typical life-only, single premium immediate annuity ("Life Only SPIA"),[12] which is designed for income only (not for liquidity or growth potential), may offer a higher rate of return during income distribution than a deferred annuity with guaranteed lifetime withdrawal benefits. On the other hand, the deferred annuity with a guaranteed lifetime withdrawal benefit option is designed to continue the contract value's growth potential.[13] The deferred annuity typically also provides more liquidity during the income distribution phase by providing access to the contract value (subject to limits during the surrender period that if exceeded can result in charges).

Individuals currently have access to many different variations of annuities which provide lifetime income guarantees. There are those designed to be used with other investment options outside the annuity itself.[14] 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 require a deferral period. Others provide greater benefits the longer the consumer waits to take income distribution, but do not make deferral mandatory.[15]

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[12] A Life Only SPIA is an annuity that pays a guaranteed income amount during the lifetime of the person covered by the protection. In a SPIA, the owner pays a single premium to the insurance company which it in turn is used to fund the guaranteed income. The insurance company bears the risk that the fund will not be sufficient to pay all of the guaranteed income. The owner has no access to the fund.

[13] A guaranteed lifetime withdrawal benefits is available on deferred fixed and variable annuities. The guaranteed lifetime withdrawal benefit provides the contractowner the option to take guaranteed income over the individual's lifetime through withdrawals from the contract values. If the contract values are depleted due to the scheduled withdrawals, the insurance company guarantees to continue the lifetime income payment. These options give an individual increased liquidity because he or she has access to the remaining balance of the contract value while taking withdrawal. However, any unscheduled withdrawals may reduce the insurance company guarantees to continue the lifetime income payment.

[14] Examples include the longevity protection product and the guaranteed lifetime withdrawal benefit wrapper. The longevity protection product starts paying a lifetime income guarantee at a specified date, usually set near the end of the annuitant's life expectancy. Prior to that age, the individual must rely on retirement income from other sources. The guaranteed lifetime withdrawal benefit wrappers are similar to the deferred annuity with a guaranteed lifetime withdrawal benefit option except that the individual's retirement savings are not held under the annuity itself.

[15] Examples are variable annuities that have guaranteed lifetime withdrawal benefit options. Variable annuities are annuities that accumulate based on the performance of selected underlying investment options. Unless there is a

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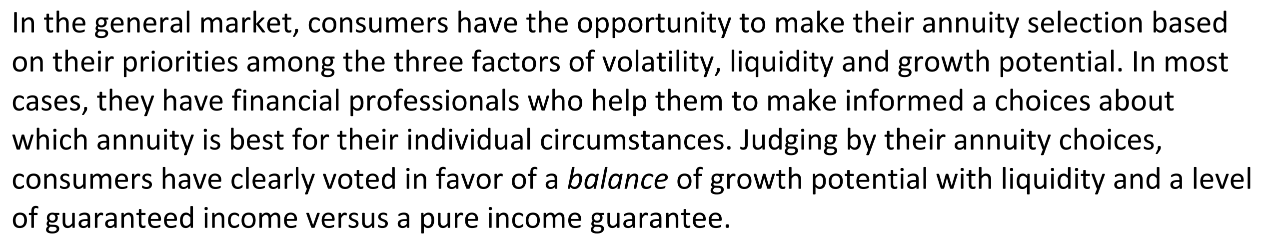

In the general market, consumers have the opportunity to make their annuity selection based on their priorities among the three factors of volatility, liquidity and growth potential. In most cases, they have financial professionals who help them to make informed a choices about which annuity is best 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.

As the Agencies are aware, some defined contribution plans do offer annuities, but most have very low election rates. Allianz believes that part of the reason 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.

II. Annuities in Defined Contribution Plans

Allianz recognizes that incorporating annuities, particularly annuities that provide the guaranteed lifetime income benefits described above, into defined contribution plans presents certain challenges. Because we expect that the Agencies will receive responses from a variety of plan sponsors providing detailed suggestions on how to incorporate lifetime income products into existing plans, Allianz will not address this issue in our response. We will, however, briefly discuss some of the challenges presented when introducing annuities into such plans.

A. Plan Provider Selection of Products

Defined contribution plans, other than 403(b) plans, generally interact exclusively with investment companies. Insurers, who are the only entities that can issue annuities, have not traditionally been included as product providers in these types of defined contribution plans.[16] As such, administration system connectivity between insurance companies and plan sponsors is generally limited.

B. Bias Against Annuities as Retirement Products

The defined contribution market was established by the securities industry and a marketplace that has historically had some degree of bias against annuities as retirement products. Allianz believes that due to the increased recognition of the importance of guaranteed income, there is

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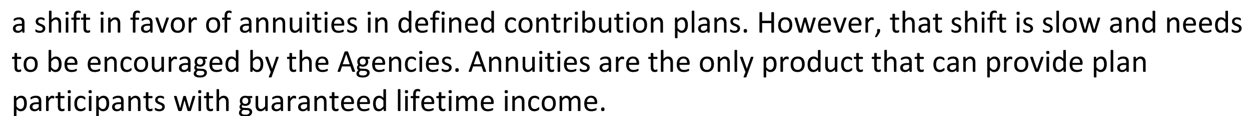
specified guarantee, these annuities have greater growth potential but come with greater volatility than fixed or fixed index annuities. When variable annuities have a guaranteed lifetime withdrawal benefit option, they typically allow an insured to start income distribution at any time. On the other hand, at its simplest, for every year the insured does not start income distribution, the income guarantee can grow by a defined percentage.

[16] To the extent that annuities are currently in the defined contribution marketplace, the products are generally more limited, as compared to annuities available in the individual marketplace.



a shift in favor of annuities in defined contribution plans. However, that shift is slow and needs to be encouraged by the Agencies. Annuities are the only product that can provide plan participants with guaranteed lifetime income.

C. **Portability of Benefits**

The issue of portability is more problematic in the defined contribution space than in the general market. Plan participants can lose their annuities when plan sponsors move to a different third party administrator that may use a different insurance carrier or may not even offer in plan annuities. The guaranteed income products discussed in Section III of this response provide consumers with certain rights that currently do not simply transfer from one insurance company to another.

D. **'Double' Deferred Taxation**

Allianz is aware that some have questioned the value of allowing a tax-deferred accumulation vehicle (an annuity) into another tax-deferred accumulation vehicle (defined contribution plan). However, as Allianz has described above, the value of the annuity is that it is the only product that can provide accumulation guarantees as well as guaranteed lifetime income options.

III. The Problem of Current Education and Consumer Perception

As stated above, Allianz believes that during retirement many consumers will need a predictable, guaranteed lifetime income from their defined contribution plans. To accomplish this goal they must first understand the importance of such an option and then have the opportunity to elect it.

According to one recent study:

> The very real possibility of living to age 90 or 100 combined with the volatility of inflation and investment returns means that the risk of outliving one's assets is quite high. Without additional guaranteed lifetime income streams, such as income provided by an annuity, middle-income Americans are at high risk of outliving their financial assets and living their final years in poverty. A greater focus on increasing retirement savings and vehicles that provide a guaranteed lifetime income stream will play a significant role in reducing the retirement vulnerability of retirees in the future.[17]

Unfortunately, planning in defined contribution plans often tends to focus primarily on accumulation versus income strategies. When a participant retires, the participant is typically advised to move money to "less risky" types of assets, and then periodically take "some" income from the assets he or she accumulated in the plan, with the hope that those assets will

[17] Ernst & Young, LLP, *Retirement Vulnerability of New Retirees: The Likelihood of Outliving Their Assets*, July 2008.

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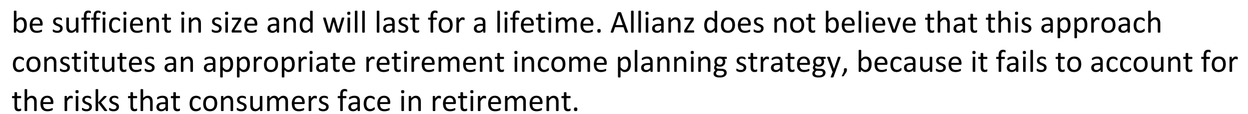

be sufficient in size and will last for a lifetime. Allianz does not believe that this approach constitutes an appropriate retirement income planning strategy, because it fails to account for the risks that consumers face in retirement.

A. Longevity Risk

One of the greatest risks consumers face in retirement income planning is outliving retirement assets. Most consumers do not understand or appreciate the magnitude of this risk, as the risk has moved from the government and the employer to the individual, due to the shift from defined benefit to defined contribution plans. Historically, Social Security and defined benefit plans were the primary source of an individual's retirement income. In that case, the government and an employer would bear and manage the longevity risk.

While an examination of life expectancy and mortality rates for defined benefits is outside the scope of this response, it is generally understood that projected mortality and life expectancy rates have not matched actual improvements in mortality and life expectancy. This has contributed to financial problems for defined benefit pension funds, individuals, and social security systems.[18] That is important to this discussion because people are living longer than was expected in retirement. As we will revisit in the discussion of the "4% Rule," below, for defined contribution plan participants, failing to adequately plan for longevity is a potentially devastating mistake.

B. Market Volatility Risk

As discussed throughout this response, Allianz believes consumers do not adequately understand the need to balance three fundamental considerations in utilizing financial products to meet the specific objectives of volatility, liquidity, and growth potential.

In the case of defined contribution plans, the volatility risk is not fully understood and can have a significant effect on the lump sum that a participant has available at retirement to convert into a lifetime income stream. An annuity is an important tool that can guard against a portion of the volatility risk inherent in market participation, while still providing opportunity for growth potential.

The protection available with annuities is particularly valuable in protecting plan participants during the several years before and after the retirement date. During this time, market volatility can be especially harmful to retirees because they have less time to recover and a larger asset base at risk.

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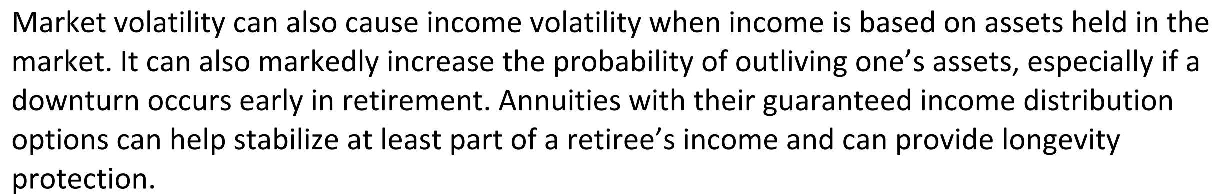
[18] Turner, J., *Mortality Improvements and Pension Liabilities*, Society of Actuaries, 2005. Antolin, P., *Longevity Risk and Private Pensions*, OECD Working Papers on Insurance and Private Pensions, 2007. "The improvements in mortality and life expectancy were unanticipated as the consistent underestimation of the actual outcomes illustrates." *Id.* at 4.



Market volatility can also cause income volatility when income is based on assets held in the market. It can also markedly increase the probability of outliving one's assets, especially if a downturn occurs early in retirement. Annuities with their guaranteed income distribution options can help stabilize at least part of a retiree's income and can provide longevity protection.

C. Current Defined Contribution Planning and Advice

In addition to the accumulation-oriented focus of defined contribution planning and advice, there has also traditionally been a bias against the very products (annuities) that can best address longevity and volatility risk.

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.

Some advisors and the media claim that "normal" investment returns on a balanced portfolio exceed the value of a guarantee.[19] Guarantees have also been dismissed as too expensive. [20]

Another root cause is the fact that annuities and lifetime income products are often compared to "equity investments." This comparison is not appropriate as each serves different purposes. Annuities are designed to minimize volatility by providing guarantees;[21] 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. [22]

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[19] *See e.g.* Farrell, C., *Should Clients Annuitize Their Retirement Assets*, Investment News (July 16, 2009); Milevsky, M., *Confessions of a VA Critic*, Research Magazine (December 31, 2006).

[20] *See e.g.* Smith, K., Soto, M., and Penner, R., *How Seniors Change Their Asset Holdings During Retirement*, The Urban Institute Retirement Policy Program (October 2009); Milevsky, M., *Confessions of a VA Critic*, Research Magazine (December 31, 2006).

[21] 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., Babbel D., *Real World Indexed Annuity Returns*, Wharton Financial Institutions Center, October 5, 2009.

[22] *Id.*

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D. The Risk of The "4% Rule"

A traditional approach to retirement income planning promoted by many financial advisors and members of the media is the "4% Rule." Quite simply, the strategy is to build enough assets during accumulation to ensure an annual withdrawal rate of 3-5% will be enough to maintain an anticipated lifestyle in retirement. This approach is designed for a typical 65-year-old male with a 20-year life expectancy, and is achieved by investing regularly, diversifying, and rebalancing. Simulations using normal market assumptions have proven that this generally works in most market scenarios. The strategy, however, fails to account for individuals who live longer than 20 years or for those who experience an unexpected market scenario in which assets would be depleted prematurely.

While this 4% Rule has become the most parroted piece of advice to retirees and pre-retirees for retirement income,[23] it is fundamentally flawed, leaving consumers depending on assets that are subject to market volatility and may or may not last for their lifetime.

In contrast, the Agencies should consider that plans and plan sponsors should introduce the concept of "sustainable retirement income planning."[24] That is, consumers should be given clear information and advice regarding how long their income stream should last and the risk of living too long relative to that income stream.

E. Consumer Perception

Allianz submits that the Agencies, in conjunction with the financial services industry and plan sponsors, should work to change the perception of guaranteed income products and educate consumers about the benefits of these products.[25] While Allianz is beginning to see a slightly more balanced dialogue in the press regarding these products, a focused and widespread education effort will be required to fundamentally change consumer perceptions, and most importantly, behavior.[26]

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[23] Currently, many defined contribution plan providers and retirement advisory organizations have pages on their websites that describe the 4% Rule; often to the exclusion of even the mention of other options.

[24] Ameriks, J., Hess, M., Ren, L., *Comparing Spending Approaches in Retirement*, Pension Research Council, October 2009.

[25] *See e.g.* Milevsky, M., *Confessions of a VA Critic*, Research Magazine (December 31, 2006); *Private Pensions: Alternative Approaches Could Address Retirement Risks Faced by Workers but Pose Trade-offs*, United States Government Accountability Office Report to the Chairman, Committee on Education and Labor, House of Representatives (July 2009); Iwry, J. Mark and Turner, J., *Automatic Annuitization: New Behavioral Strategies for Expanding Lifetime Income in 401(k)s*, The Retirement Security Project (July 2009); Farrell, C., *Should Clients Annuitize Their Retirement Assets?*, Investment News (July 16, 2009); Smith, K., Soto, M., and Penner, R., *How Seniors Change Their Asset Holdings During Retirement*, The Urban Institute Retirement Policy Program (October 2009); Ameriks, J., Hess, M., and Ren, L., *Comparing Spending Approaches in Retirement*, Pension Research Council Working Paper, Univ. of Penn. Wharton School (October 2009).

[26] *See, e.g*. Lankford, K., *Lock in Your Retirement Income*, Kiplinger's Personal Finance, May 2010.

IV. Actions Recommended to the Agencies

A. Encourage Annuities Though Income Product Availability and Needs Education

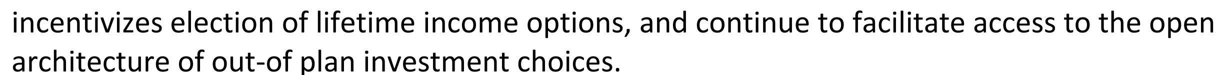
Allianz strongly encourages the Agencies to adopt Rules that require plan sponsors to include educational materials that meaningfully describe properly designed annuities with accumulation guarantees as well as lifetime income solutions.[27] In addition, the Agencies, working with the financial services industry and consumer advocacy groups, 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.

Retirement planning should be facilitated and encouraged with incentives so that plan participants take action to pro-actively provide for their future. This should include education on providing lifetime income protection in their retirement. This should also include education on risks plan participants face during retirement and how best to protect themselves. This education and planning should ensure that plan participants' individual priorities towards the three fundamental factors (volatility, liquidity and growth potential) are considered in any selection of investment options or financial purchases. Given the complexity of this planning, the use of professional financial guidance should be encouraged so that plan participants can make well-informed decisions and take appropriate action.

At the very least, education about retirement planning should be part of participant enrollment, available during the accumulation phase and at time of any distribution. Allianz does not believe that a consumer should have the form of their income protection prescribed; rather, as individuals' needs vary, participants should have flexibility to choose an annuity if appropriate to their needs.

With the focus on protecting from longevity risks, there may be a proposal to mandate a default lifetime income option. Allianz believes that 'defaulting' investors into a generic lifetime income option may not produce the intended result. Investors defaulted into a lifetime income option not based on their individual needs may be more likely to ultimately elect a lump sum withdrawal option. Allianz believes that the Agencies should encourage product innovation that

[27] The Retirement Security Project discussed the impact of how the discussion is framed. The "consumption frame" uses terms like "spend and "payment," mentions only the amount of money generated each month, and keeps the underlying financial details (like rate of return) opaque to the individual. By contrast, the "investment frame" uses the terms "invest" and "earnings", explicitly mentions rate of return, describes the potential for early withdrawal, and characterizes the final investment value upon death for a set of different financial products, including both life annuities and savings accounts. Brown, J., Klings, J., Mullainathan, S., and Wrovel, M., *Why Don't People Choose Annuities? A Framing Explanation*, The Retirement Security Project (March 2008).



incentivizes election of lifetime income options, and continue to facilitate access to the open architecture of out-of plan investment choices.

B. Encourage Annuities by Continuing to Support Out-Of-Plan Choices

Allianz believes that investors 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 respectfully 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.

The use of in-plan options has a number of limitations. First, the selection of an annuity provider by a plan necessarily results in limiting choices of both the product and insurance company available to plan participants. This not only limits the participant's choice but also limits the education that a participant will receive regarding the range of guaranteed lifetime income options. Second, because of the sponsors' efforts to avoid fiduciary liability, in-plan education seminars are often generic, and do not focus on the individual needs of the participants. Third, in-plan annuity options may be disfavored by participants in plans where there is a lack of portability.

Allianz submits that many of these problems do not exist with respect to out-of plan ("roll-over") options. 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. Out-of-plan options 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. Out-of-plan annuities are, in effect, an open-architecture selection opportunity for consumers, allowing individuals to choose the annuity provider and annuity product that meets their needs.

C. Technical Changes that May Facilitate Further Product Design and Lifetime Income Adoption

1. Changes to the Required Minimum Distribution Rules

In order to make guaranteed income solutions more attractive in the marketplace, many insurers are developing a broader range of options. However, if the rigid annuity-based distribution rules set forth in Treas. Reg. § 1.401(a)(9)-6 are the only rules that can be applied to an annuity contract, the development of innovative annuity contracts may be stifled. This may cause a decrease in the desirability of annuity contracts as a means of accumulating assets

and providing an income that will last a lifetime. These rules interfere with an individual's need to plan for their unique circumstances and retirement needs.

2. Changes to the Joint and Survivor Annuity Requirements

As a result of the potential application of the complex joint and survivor annuity requirements set forth in IRC §§ 401(a)(11) and 417, many sponsors of defined contribution plans have been reluctant to provide life annuities as an option under their defined contribution plans.[28] It is unclear whether the addition of an annuity option and the allocation of plan assets to the annuity during a participant's working career (and before income distribution) will be treated as the election of a life annuity thereby implicating the need to meet the joint and survivor annuity requirements at the time of the contribution or allocation.

The joint and survivor regulations should be clarified so that the addition of an annuity option to a plan's investment choices and the election by a participant to either contribute to the annuity option or transfer existing balances to the annuity option is not treated as the "election" of an annuity at the time of contribution or allocation within the meaning of IRC § 401(a)(11)(B)(iii)(II).

Conclusion

Allianz thanks the Agencies for their inquiry into this important issue. 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 under-emphasize retirement income. Defined contribution participants should have open, free 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 a distribution from those funds.

Allianz believes that 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.

[28] Treas. Reg. § 1.401(a)-(3), Example (1) provides that if a plan provides a life annuity option as a benefit distribution option, the plan must be amended to provide that if a participant elects a life annuity option, the life annuity benefit will be paid in a form having the effect of a qualified joint and survivor annuity unless the participant elects another form of benefit payment.