U.S. Senate Finance and HELP Committees Joint Forum
"Private-Sector Retirement Savings Plans:
What Does the Future Hold?"

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(Submitted March 24, 2005)

Thank you for organizing this important forum and inviting me to participate on behalf of Genworth Financial. With 15 million valued customers, more than 5,000 skilled professionals, and more than $103 billion in assets (as of December 31, 2004), we are one of the world's largest insurance organizations. We serve three major customer needs: protection, retirement income and investments, and mortgage insurance.

Introduction to the Problem

Helping Americans improve their ability to enjoy a financially secure retirement is one of the most challenging domestic issues faced by this Congress. Americans are spending a greater portion of their lifetimes in retirement than previous generations. Today, more than half of all workers retire before their 62nd birthday, and the average retiree can expect to spend approximately one-fourth of his or her life in retirement. Retirement is also the most difficult financial planning exercise that the average individual will face in his or her lifetime because the stakes are so high - the potential consequence of making a mistake is to live the last years of one's life in poverty.

A comprehensive retirement income system should be built to deliver results on all facets of the "Three-Legged Stool": Government Social Security, employer sponsored plans, and individual personal savings. As the focus of this forum is the trend in employer sponsored plans, it is important to recognize the degree to which the burden of assuring an adequate retirement income is shifting to the individual, who typically has not been given the tools to meet this challenge. This shifting to the individual of responsibility for a financially adequate retirement will continue as long as the availability of traditional Defined Benefit (DB) plans continues to decline. Employees are faced with a loss of guaranteed income during retirement and they have limited options in replacing that "paycheck" for life.

Further exacerbating the problem of achieving an adequate retirement income is the simple fact that Americans are living longer. A longer life is something to be thankful for, but it means that we each will need income that will match that longer lifespan. Today, 50% of healthy 65-year-old women will live past age 85. In fact, one in three will live past age 90 and one in 10 will live past age 95. In addition, women spend even more time in retirement than men and are less likely to have participated in employer sponsored retirement plans. Forty-four percent of female workers lack a pension from any employer, compared to 36% for male workers. These factors mean that both men and women face a difficult challenge in managing their savings during retirement years.

The Lack of Guarantees for the Individual

At the center of the challenges and concerns individuals have about their retirement security is the lack of guarantees, in particular the lack of a guaranteed income that will last regardless of how long the individual lives and no matter how the stock market performs.

In their current design, Defined Contribution (DC) plans do not replace the guarantees that are associated with a traditional DB plan. There is no guaranteed minimum income, there is no guarantee that the retirement income will last a lifetime, and there is no guarantee on the performance of the individual's overall retirement portfolio. Without these guarantees, the employee is faced with having to mitigate six key retirement risks on his or her own. These six key risks are:

- long-term rate of return risk (will your assets perform as expected),
- inflation risk (will your returns outpace inflation),
- excess withdrawal rate risk (how much can you safely withdraw),
- point-in-time risk (can you weather a down market at the time of retirement),
- longevity risk (will you outlive your assets), and
- health care risks (will your income stream support rising healthcare costs).

Potential Solutions

Life insurance companies are in a unique position to help employees manage these risks by partnering with DC plan sponsors and mutual fund companies. Life insurance companies can pool longevity and investment risks across a large number of participants – thereby providing guarantees at the individual participant level. These guarantees are provided by financial institutions that are highly regulated by the states to assure that individuals receive the benefits they have been promised.

There is widespread recognition that the purchase of income annuities, "annuitization," at the point of retirement would help mitigate some of these risks. It is a common practice for life insurance companies to:

- convert an account balance into a guaranteed income stream that will last a lifetime,
- offer guaranteed payouts over the life of a single individual or the life of the individual and his or her spouse,
- increase a fixed payout stream for an expected inflation rate,
- guarantee that payments will continue for a minimum period whether the individual lives or dies, and

- allow the individual to participate in equity market performance.

As a consequence, an emerging market is developing in what Genworth calls "Insured Defined Contribution" plans. Insurance companies like Genworth, MetLife, and others are building new annuity products that allow sponsors to offer defined benefit investment options to their employees within a 401(k) plan. The importance of an Insured DC option is that the individual throughout his or her working career, without having to wait until retirement, is able to determine with certainty how much guaranteed lifetime income his or her current 401(k) account balance will buy at a future retirement date.

An Insured DC option can be made portable, thereby addressing the issues created by an increasingly mobile workforce. In addition, some designs can be structured to provide upside potential through equity participation in order to offset the risk of inflation. Our consumer research into the Insured DC option has indicated significant interest on behalf of 401(k) participants. Here are the highlights of our findings:

- 69% of participants age 25-34 would invest in an Insured DC offering if given the opportunity; 70% of all participants would do so.
- 23% of those who say they would invest in an Insured DC option would increase their contributions to their 401(k) plan if able to participate in such an option.
- 54% of the individuals who choose not to participate in their employer's 401(k) plan would participate in the plan if an Insured DC option was available.
- 95% of participants found the guaranteed minimum income for life feature of an Insured DC option attractive (63% said very attractive).
- 93% of participants said portability of the Insured DC guarantee was attractive (53% said very attractive).

The Need for Education

A key predicate to successfully managing the risks that Americans face in retirement is making sure that they understand those risks. Most Americans have not had the opportunity to prepare for the responsibility they will face at retirement. Financial planners report confusion about retirement planning and many working people do not understand how to convert assets into enough income to cover a lifetime of non-discretionary expenditures. This conversion of account balance into lifetime income at a future retirement date is a very sophisticated calculation. In order for Americans to understand the dynamics of this retirement reality, we as a country must address the significant education gap that exists today.

The following simple question illustrates the complexity in this area: If you were 65 today and were to retire today, would you feel wealthier if you had $500,000 in your 401(k) plan or had a pension guaranteed to pay you and your spouse $32,500 per year for the rest of your lives? It becomes a harder question to answer when given the added information that many advisors would say that no more than $20,000 should be withdrawn annually from a $500,000 balanced fund in order to be reasonably assured that the money will last 30 years. However, even at this safe withdrawal rate, there is no longevity or investment performance guarantee, so it is still possible to outlive this money.

To help Americans understand the retirement security issues they face and the solutions available to them, retirement education needs to focus on three components:

- the basics of personal finance, including the discipline of saving, starting to save early in your working life, and the value of compound interest,
- the conversion of savings into a reliable income stream, and
- the value of guaranteed income, a "paycheck for life," and the benefit of pooling longevity and investment risk with others.

While many valuable financial education initiatives have been undertaken in recent years by both the public and private sectors, more can and should be done.

The Importance of Life Contingent Annuities

One of the most important, and often least understood, sources of financial risk comes from uncertainty about how long one will live. According to a 2001 study by the Society of Actuaries, 67% of retired women and 55% of retired men underestimated the average life expectancy of a 65-year-old. This uncertainty means that there is a real risk of experiencing a reduction in living standard at older ages, even if one has tried to prepare for retirement. Saving is not enough; one must also be a careful manager of one's savings. Individuals should be encouraged to manage their savings during retirement in a manner that accommodates their daily needs, but also ensures that their savings will not be exhausted when they have more years to live. This is why life contingent annuities are so important.

An annuity that continues to make payments for as long as you live (often called a "life contingent" annuity) is an affordable, powerful retirement tool that allows individuals to manage many of their personal retirement risks. The life contingent annuity is a combination of investment expertise and insurance that gives individuals the ability to insure against the financial risks of retirement by pooling their assets, and their financial risks, with a large number of other policyholders.

For many individuals, guaranteed lifetime income payments from an annuity may be the most effective way to ensure that retirement savings will not be depleted during their life. Outside Social Security and employer sponsored DB plans, only an annuity can guarantee that an individual will receive regular, guaranteed income payments for as long as he or she lives.

A life contingent annuity is designed specifically to address the financial planning problem of guaranteeing that individuals will not outlive their income no matter how long they live. The annuity can be designed to give consumers the flexibility to transform accumulated savings - both savings inside an employer plan and those accumulated outside of a plan - into a variety of forms of guaranteed streams of retirement income based on each individual's needs.

Annuities have a variety of features and options that allow individuals to provide for their own retirement needs and to provide for a spouse or heirs after death. The payment stream itself can take a variety of forms depending on the individual's needs. It can guarantee payments over a person's life (a life contingent annuity), over two peoples' lives (called a joint and survivor annuity), over a specified period (called a period certain annuity), or over a life or lives with a minimum period of payments guaranteed, *e.g.*, 10 years (called a certain and life annuity). Annuities that combine life contingencies with period certain features are particularly attractive because they protect against longevity risk while at the same time providing the ability to bequeath amounts to heirs (either in a lump sum or as continued periodic payments) upon a death during the period certain.

Annuity payment streams can be designed to make fixed income payments (called a fixed annuity), or can be designed to protect against inflation by making payments that increase or decrease with market performance (called a variable annuity). Some variable annuity products also guarantee minimum income levels while providing the upside potential of the equity markets, thereby protecting against investment risk in addition to inflation and longevity risk.

The key point is that life contingent annuities, in whatever flavor may best suit a particular individual's circumstances, provide individuals with the guarantee of an income stream that will continue throughout their retirement years, no matter how long they live.

Conclusion

The combination of more and improved retirement education, the growth of Insured DC options in employer plans, and encouraging more individuals to manage retirement risk through life contingent annuities would benefit the Three-Legged Stool: employers would have a predictable and stable funding vehicle for the retirement benefits they offer and have employees that value and appreciate the benefits offered; employees would have an option for guaranteed retirement income for life and would be motivated to begin addressing the concern earlier in their working lives; and the government would have the other two legs of the stool helping to bear the load of retirement security.

Once again, we appreciate being included in this timely forum and look forward to discussing the many different alternatives available to resolve some of these critical retirement savings and income issues faced by our country.