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10400 Viking Drive, Suite 190
Eden Prairie, MN 55344
Phone: (952) 941-5351
Fax: (952) 941-5744

**Hueler Companies**

**Written Statement for the Record**

**for**

**"The Retirement Savings Challenge: Making Savings Last a Lifetime"**

**Before the**

**United States Senate Special Committee on Aging**

**June 16, 2010**
**2:00 p.m.**
**Dirsken Senate Office Building, Room 562**

**Hueler Companies Written Statement for the Record**
**"The Retirement Income Challenge: Making Savings Last a Lifetime"**
**Senate Special Committee on Aging**
**United States Congress**
**June 16, 2010**

**Kelli Hustad Hueler**
**President and CEO, Hueler Companies**

I want to thank you for holding this important hearing and for inviting Hueler Companies to provide testimony on such a critically important issue. We are grateful to Chairman Kohl (D-WI) and Ranking Member Corker(R-TN) for their willingness to address the challenge of ensuring retirement income sufficiency for millions of Americans.

By way of background, Hueler Companies was founded in 1987 as an independent consulting firm assisting plan fiduciaries and trustees with research, product selection, and ongoing oversight of their stable value investment funds. Our hallmark has been independent research, analytical reporting, and continued efforts to improve transparency through standardized reporting. Today Hueler Companies acts as an independent source of industry data, market research, analytical reporting, and related services to all major market segments. The Hueler Analytics Pooled Fund Universe tracks approximately 85% of professionally managed stable value pooled funds. The Universe constitutes approximately $100 billion in assets representing close to 40,000 retirement plans.

In 2000, Hueler Companies pioneered the development of a web-based platform that facilitates efficient, transparent, low cost delivery of lifetime income annuity options to *transitioning employees,* those employees at, near or in retirement. The broader mission of this effort was to create a platform that transformed annuity delivery to plan participants by leveraging the institutional purchase process, eliminating the inherent conflicts of interest, and allowing for open affordable access to all plan sponsors. After several years of research and development directly with plan sponsors and annuity providers, Hueler launched the Income Solutions® annuity program in 2004. In July of 2005, Hueler provided testimony before the ERISA Advisory Council Working Group on Retirement Plan Distribution Options.

To date over 1,000 plans have adopted the Income Solutions® program in order to extend access to lifetime income alternatives to*transitioning employees*. It is important to note that, while the program was designed to facilitate implementation as either an in-plan distribution option or a voluntary IRA rollover, 98% of plans choose the voluntary IRA rollover distribution alternative. We will comment further on survey data gathered around why this is the case. Adoption is generally facilitated through large plan administrators, as integration with the existing benefits portal is optimal (three of the top six plan administrators and six of the top 17 plan administrator firms are currently providing access to the program). Based on new adoptions scheduled for 2010 these numbers will continue to show meaningful growth. Access to this alternative is currently offered to millions of participants. Monitoring activity and analyzing actual results, both positive and negative, has afforded us the opportunity to observe what does and does not work, identify continued roadblocks, and develop solutions for improved utilization.

Our experience throughout the last decade in working with a variety of plan administrators, plan sponsors, and participants will be the basis for my comments today. I hope to offer insights from our direct experience and empirical data we have compiled. My comments will address five important areas of consideration: 1) Participant behavior and decision making, 2) The benefits of utilizing an institutional delivery framework, 3) Mitigating key financial risks for participants, 4) Plan Sponsor behavior and decision making, and 5) The role of technology.

It is also worth noting that Hueler does not manufacture any form of investment or insurance products, so we are neutral to the actual product type and structure. However, our interest and experience is with those products that provide guaranteed lifetime income, lend themselves to transparent comparison, can be selected based on competitive results, and are delivered at low cost.

**Participant Behavior and Decision Making**

Industry statistics show that plan participants rarely select annuitization options out of their defined contribution plans and a majority of plan sponsors report that participants rarely ask for annuities. While this may be factual information, it does not offer any insight as to why there is such a low take up rate for annuities among participants and why plan sponsors have largely eliminated the option from their plans.

There is a fair amount of behavioral research that points to why people would choose lump sums over a stream of monthly payments (desire for control, a chance to buy their dream, belief that they can do a better job managing the money, issues of trust, fear of the unknown, etc..). We refer to the obvious lump sum payment preference as the "lottery affect." Bottom line: participants are put in a very similar position as a lottery winner. In most cases, they are offered a check for more money than they have ever seen or hoped to have at their disposal in their lifetime. They are faced with the decision of taking the lump sum, having control over their money, and living their dreams, or letting someone else decide how much of "their own" money they will be allowed to have each month.

Adding to the "lottery affect", the annuity being offered typically comes in the form of an all or nothing proposition. Hueler has surveyed groups of participants and professionals from varying walks of life in forums across the country and the results are consistent. When we describe the choice of receiving a lump sum check that individuals can use to make decisions as they see fit in the time frame that makes sense for their lives versus transferring the entire balance of their life savings to a single source in return for monthly payments for the rest of their life, typically only 1-2 % of the group responds affirmatively. Depending on the audience, the responses may be as low as zero or as high as 5%. At a minimum, plans should be strongly encouraged to allow for partial distributions.

In our experience it is not the annuity or lifetime income alternative that participants react negatively to, it is the packaging and method of delivery. Interestingly, when you change the proposition and give the audience a more flexible set of options, as outlined below, the results radically improve. At least 1/3 of the group typically answers affirmatively and in some cases up to 2/3rds can be expected to do so:

Flexible Proposition

1) The option to decide how much money to set aside for lifetime income payments using only a portion of their savings and leaving the balance in their plan
2) Individuals decide when to begin receiving payments
3) Competitive low cost quotes not available after you leave the plan
4) Multiple insurance companies to choose from
4) Quotes are customized to reflect personal income needs
5) Inflation protection is an option
6) Indviduals can buy from more than one company
7) No obligation to purchase

Another key contributing factor is that participant education has been virtually devoid of references to lifetime income for several decades. In most cases, the communication and education provided has focused on the benefits of saving more, taking investment risk, having a long-term horizon, dollar cost averaging, and to some extent, preserving principal. Taking steps to appropriately “pensionize” retirement savings is largely a foreign concept for baby boomers, yet they are now facing critical decisions about securing income for life. The decisions made at this juncture could have substantial impact on an individual’s ability to sustain themselves financially for the duration of their lives.

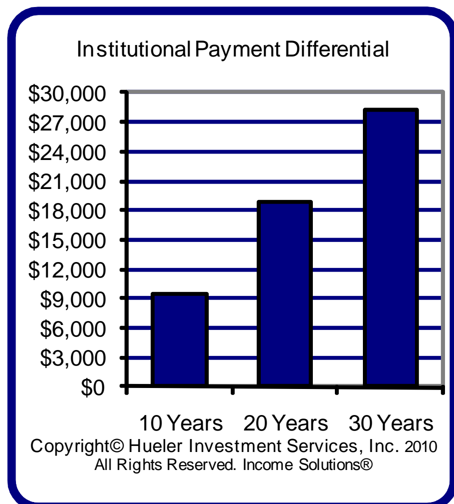
Finally, you cannot underestimate the natural inclination to take the “path of least resistance.” The lump sum payout is infinitely easier to choose for the reasons outlined above and other additional perceived constraints.

Unless changes are made to the packaging, delivery method, and education practices around annuitization and lifetime income alternatives nothing will change. Plan participants will not properly pensionize their retirement savings and will remain at significant risk.

## The Benefits of Utilizing an Institutional Delivery Framework

If annuity products are purchased after a participant leaves the plan they will likely be retail arrangements and will not offer the same benefits provided by institutionally delivered products. Commission based planners and captive agents offer products that encourage assets to flow out of low cost employee sponsored retirement plans into higher commissioned products. High costs will have a substantial negative impact on the value of an individual’s retirement savings and will conversely limit the total income available over a 20-30 year period.

The illustration below shows the approximate financial benefits an individual may expect to receive when institutional pricing and competitive quoting are combined.




For example, a $200,000 single life only annuity for a 65 year old male resulted in a monthly payment of $1,311 when purchasing an annuity through the Income Solutions® program versus $1,232 a month when buying a traditional retail annuity. This example is a difference of 6.4% or a $79 increase in your monthly income. Over a 10 year period this differential equates to $9,500, over 20 years it is approximately $18,900 and over 30 years the difference grows to $28,400. Depending on the type of annuity and data provided, monthly income amounts for competitively bid, institutionally priced annuities are typically higher than the monthly income amount provided by retail priced annuities.

*(This data is based on Hueler's independent research from February 2010. Actual pricing will be dependent on each individual's quote information, market conditions and sponsoring organization. While institutional pricing is typically more competitive than retail pricing, this may not always be the case. No time value of money was factored into the differentials shown on the graph so it is a conservative depiction.)*

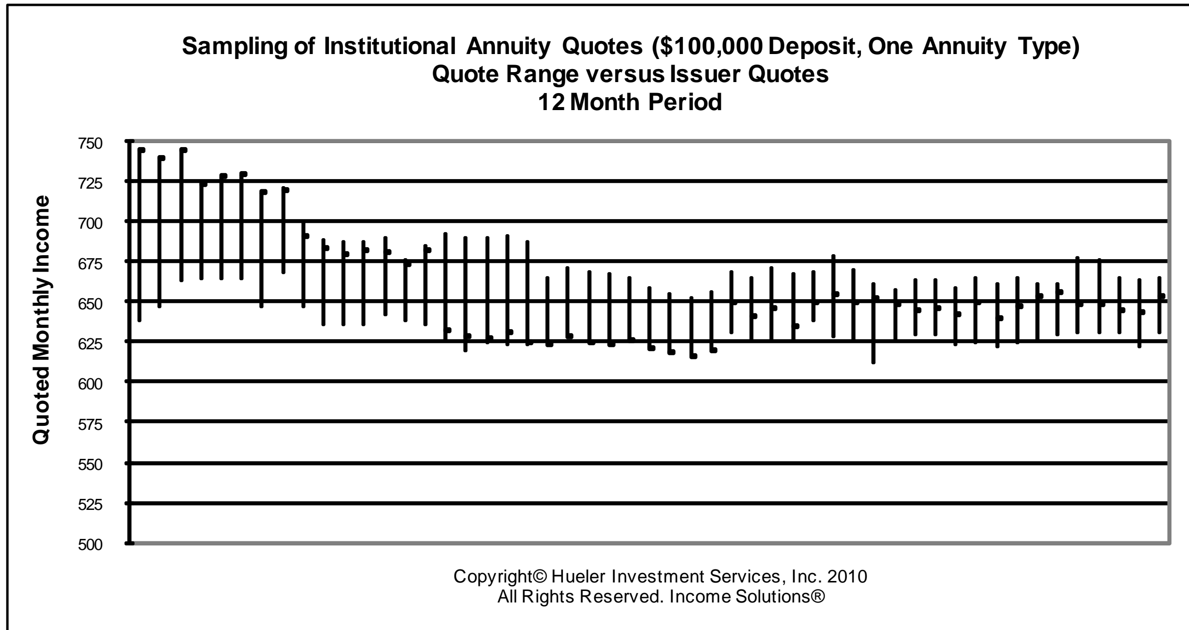
In addition to the above data, Hueler conducted a 12 week analysis of institutional annuity quotes versus five possible annuity retail offerings for a $100,000 annuity. The results showed on a consistent basis that institutional quotes produced higher monthly income amounts than those available in the retail annuity market. When comparing institutional quotes to five retail sources on over 400 individual annuity quote scenarios, the average difference showed a 6.37% advantage over the retail sources. It is important to note that the maximum difference was in the double digits (approximately 15%) from a single provider retail offering. Over time, these differentials significantly impact the guaranteed income individuals receive.

When lifetime income and annuity products are provided through employers, they should be delivered through an institutional framework. This includes institutional pricing, the benefit of due diligence for issuer selection, fee transparency, objectivity, unbiased education, and competition. Pricing data shows the variability of insurance company pricing can create substantial differentials between issuer quotes. This data speaks volumes about the potential impact on lifetime income results for individual participants.

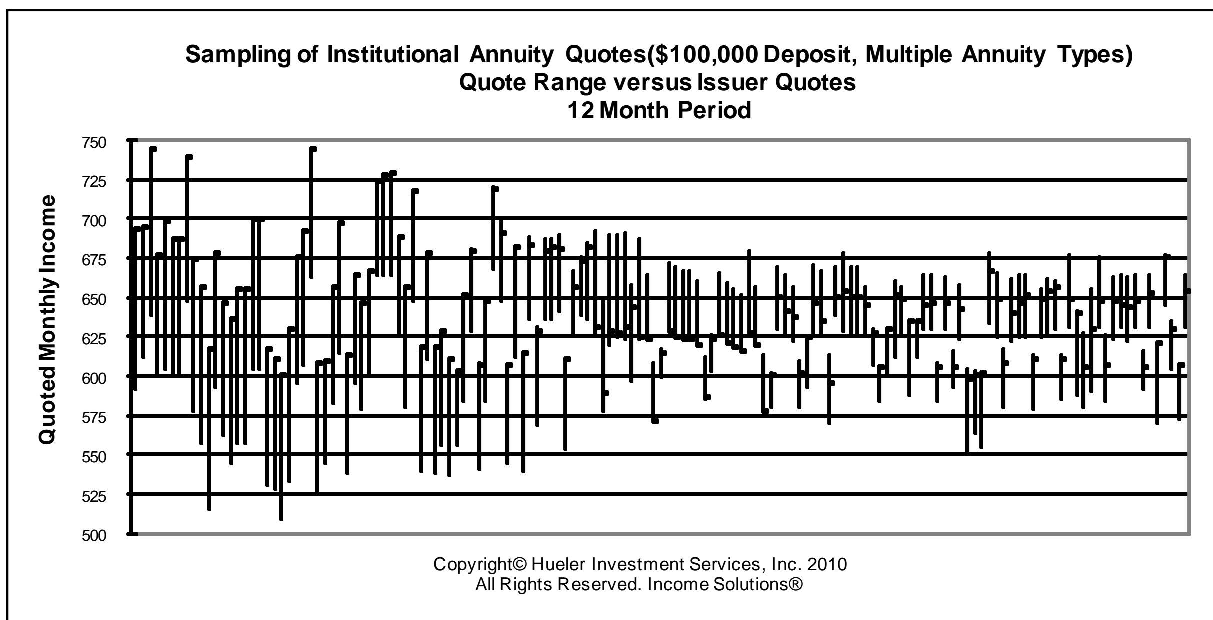
Institutional or group pricing is only part of the equation. Without competition, individual participants could have vastly different outcomes relative to how competitive the lifetime income amount is at the time they decide to retire. Competition ensures each participant will benefit from the best possible market pricing at the lowest possible cost and will be able to maximize their income amount for life.

The two charts below illustrate the variability of one individual insurance carrier’s pricing across random quote scenarios of multiple insurance carriers.

This first graph illustrates one individual carrier's quote position against multiple insurance providers for one specific annuity type over a 12 month period. Each line represents the range of the high to low annuity quotes across multiple insurance providers for each scenario. The box represents the same individual insurance carrier across each quote scenario.




The second graph expands the data from above to include a broader sample of annuity data containing multiple annuity types. The graph illustrates one individual carrier's quote position against multiple insurance providers for multiple annuity types over a 12 month period. Each line represents the range of the high to low annuity quotes across multiple insurance providers for each scenario. The box represents the same individual insurance carrier across each quote scenario.



## Mitigating Key Financial Risks for Particpants

There are significant financial benefits for participants who use some portion of their retirement savings to create a supplemental "paycheck for life" using an institutional framework to guarantee a baseline level of income. Converting some percentage of retirement assets into guaranteed income at the lowest possible cost will increase the likelihood that retirees will not outlive their assets and allow them to transfer some of the serious financial risks they face in retirement to a qualified third party. There are three primary risks to consider:

1) Longevity risk: It is a well-established fact that people are living longer than the previous generation and this could significantly increase the number of years an individual lives in retirement. Increased life expectancy is a wonderful, albeit expensive gift with new risks both known and unknown. Establishing a baseline income level, preferably one that adjusts either partially or fully for inflation, guards against the risk of outliving one's retirement savings and increases likelihood of income sufficiency.

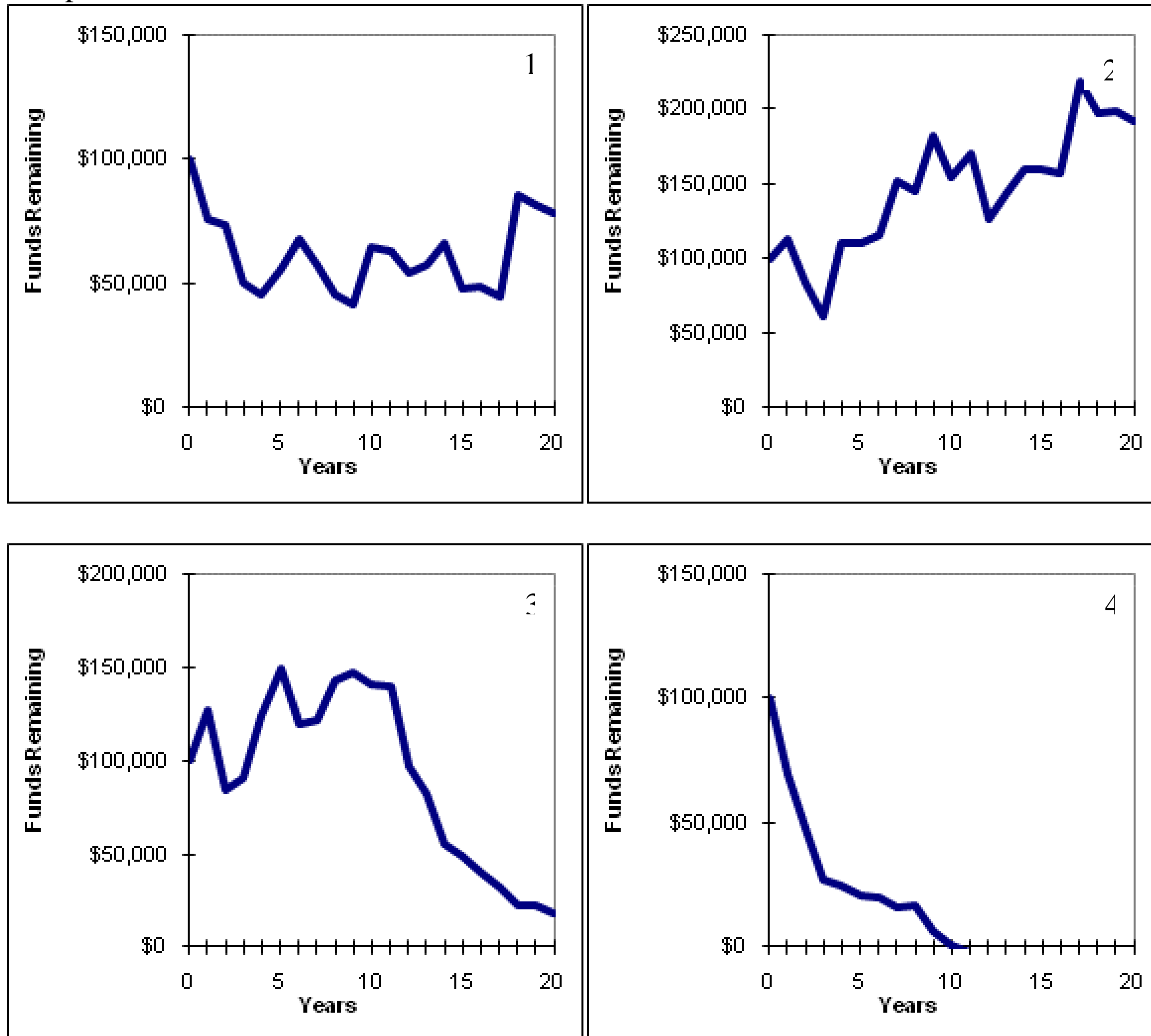
2) Investment risk: After the market correction that began in 2008, investors were stunned by the market losses they suffered. Many participants saw their retirement savings fall dramatically. For those participants who had not begun drawing down their savings as a necessary supplement to their retirement income, the situation was less dire because they may still have a chance to dollar cost average more savings into the market and recover over time. For those participants who needed to begin drawing down their balance to supplement income or had already begun drawing down their savings, the effect will have lasting and yet undetermined affects. In the first quarter of 2009 we saw quote and purchase volume through the platform increase by four times from the first quarter of 2008.

Through a random simulation of returns, the following charts help show dramatically different outcomes for the same drawdown strategy and risk profile. The graphs below illustrate the vastly different portfolio outcomes given the sequence of returns and the timing of when they occur during the drawdown phase.

The difference in outcome is based on when the timing of a given return sequence occurs during the draw down phase.

Chart 1 and 2 demonstrate how an individual portfolio experiencing positive returns early in the drawdown phase could stay at the same value or increase over time. You can see in charts 3 and 4, how negative returns early in the drawdown phase can have devastating effects. These two scenarios could leave a retiree with only a subsistence income level due to a severely reduced asset base or possibly devoid of any remaining financial resources long before their average life expectancy.

Assumptions:
Lump Sum: $100,000 Withdrawal: $4,000 Return: 4%

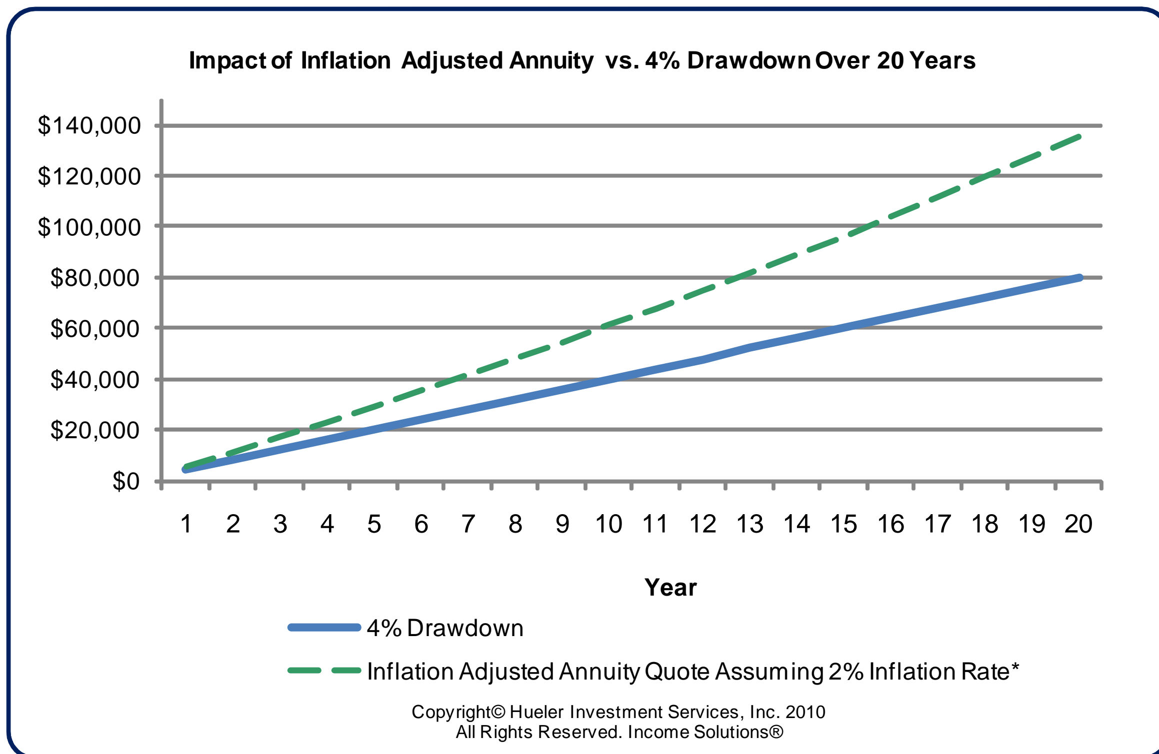



Savage, Sam. "An Annuity Example." The Flaw of Averages. 8 October 2000. Web. 27 April 2010 http://analycorp.com/SJM-animations/[1]

3) Inflation risk: Erosion of buying power over time seems to resonate with most participants at or in retirement. In fact, it is one of the justifiable deterrents to and concerns often expressed about buying a fixed annuity that does not adjust for inflation. Unfortunately, the conventional wisdom espoused by many investment professionals has been that if you invest in equities (increase your risk profile) over time your returns will outpace inflation. The 4% drawdown method has been promoted vigorously for years by the financial planning and retail brokerage community. Participants/retirees have been led to believe that this is sustainable and that such risk taking will likely mean their investments will keep pace with inflation.

The current monthly income amount for a $100,000 Single Life Only 65 Year Old Male for an inflation-adjusted annuity is $464.49 or $5,573* for the first year.[2]

The traditional 4% drawdown method on a $100,000 would result in $4,000 per year. Assuming a constant amount of $4,000 per year in comparison to the inflation adjusted annuity at an assumed 2% annual rate of inflation, the difference in income payments over 20 years is substantial.




Consider the basic pros and cons for each option:

**4% Drawdown on $100,000 = $4,000 per year**

- Market Risk (Potential Loss of Principal)
- Longevity Risk
- Inflation Adjustments Unknown
- Potential for Market Gains
- Potential for Remaining Assets Available for Heirs

**Inflation Protected $100,000 Single Life Only Annuity = $5,573[2] first year and annual minimum lifetime payment**

- Above Risks are Eliminated
- 46% Increase in Initial Monthly Income
- Annual Inflation Adjusted Income Increase
- No Remaining Assets Available for Heirs
- Provider risk

**Plan Sponsor Decisions/Behavior**

EBRI's 2010 confidence survey[3] shows that participants place a higher degree of confidence in private employers than other large institutions, insurance companies, banks, and Federal Government. However, the vast majority of sponsors are reluctant to offer education about or access to lifetime income or annuity products due to the perception of liability. With the decline of pension plans and the inherent limits of Social Security, the burden of responsibility for income sufficiency in retirement is rapidly shifting to individuals, yet their most trusted source is hamstrung and unable to participate in essential education.

The conundrum is that plan participants will not get comfortable with lifetime income or annuity options until plan sponsors are free to do a better job of educating, communicating, encouraging consideration of, and providing access to low cost competitive solutions. Information about lifetime income alternatives needs to be fully integrated into the normal flow of 401(k) investment communication and prominently displayed in the distribution process. It is imperative that individuals are encouraged to consider cost effectively "pensionizing" a portion of their retirement savings when they are still affiliated with their employer-sponsored plan.

Data compiled by Hueler shows a direct correlation between sponsor communication efforts and increased site activity. This typically holds true for both annuity quote activity and purchase activity. When a plan sponsor communicates specific information about the benefits of the annuity program, activity typically increases for a period of up to two to three months following the specific outreach. Consistent quarterly communication will boost awareness and consistently increase activity. Without practical clear guidance, however, the vast majority of plan sponsors will not be willing to offer important communication and education about lifetime income alternatives.

This issue has become very polarizing for sponsors, consultants, and product providers. In many cases, ERISA counsel recommends against providing any type of distribution option even when the sponsor is inclined to do so. In some cases, we have seen counsel rebuke consultants for recommending that the plan sponsor client even consider providing access to lifetime income on a voluntary basis.

Based on results compiled from surveying organizations currently using the program and discussions with plan administrators, plan sponsors, consultants, and ERISA attorneys, we know that the primary concerns about offering an annuity arrangement (even outside the plan as an IRA rollover) are: "potential fiduciary liability" and the "appearance of endorsement". A good indicator of these concerns is the fact that 98% of plans who adopt the program choose to implement it as an IRA rollover or voluntary distribution alternative rather than an in-plan option even though the program can accommodate either. The second most commonly cited concern is related to fiduciary liability but separately articulated as issuer selection. Our survey results show that for over 90% of plan sponsors there are three key reasons for adoption of the program: 1) it is an IRA rollover alternative rather than an in-plan option, 2) the qualified third party objective issuer selection process, and 3) the competitive multi-issuer format.

It is worth mentioning that even when a plan administrator or plan sponsor has chosen to offer access to the program they are often required to create a disclaimer page that participants must acknowledge before requesting quotes to avoid the perception of "endorsing" the program.

When this is the case, we see more than a 50% drop off rate after participants see that their employer **does not** endorse the program. The disclaimer may as well be a large "Danger Proceed with Caution" sign.

Plan sponsors will not change their behavior until there is a safe harbor for issuer selection that reflects legitimate fiduciary responsibility, but takes into account the increasingly complex industry landscape. The recent meltdown of the financial markets, the fact that some of the most prominent financial and insurance institutions fell prey to unanticipated consequences, and the failure of the public rating agencies to render credible ratings decisions before or after the crisis, leaves few plan sponsors willing to take on the fiduciary liability associated with issuer selection. Plan sponsors who are willing to utilize outside expertise either directly or through a qualified third party should be encouraged to utilize independent due diligence to meet their fiduciary obligation. As an example, Hueler augments its internal research and expertise with independent research from ALIRT, an organization that specializes in insurance company analysis (http://www.alirtresearch.com). Costs associated with independent insurance company analysis and due diligence for the purpose of performing or assisting with issuer selection should be considered a legitimate plan expense, as it directly benefits participants.

## The Role of Technology

Technology is essential for creating an efficient delivery framework for basic annuitization and other lifetime income products on a cost effective basis. Plan sponsors cannot individually afford to manage competitive bidding programs or develop and maintain internal operations sufficient to facilitate efficient delivery of these products. Acceptable, independent, and automated platforms should be easily accessible to plan sponsors and designed to ensure:

1) Competition
2) Organized product comparability
3) Fee transparency
4) Objectivity (no pay to play provider conflicts)
5) Best case pricing (low cost delivery)
6) Flexibility (staged annuitization and issuer diversification)
7) Reporting oversight

This type of platform should provide simple on-line tools that allow people to determine if they have an "income gap" and what they need to set aside to cover that gap. These tools help provide answers to questions about how much a participant should annuitize and how much income they need to cover baseline expenses. The Income Gap calculator and the Income Calculator at Hueler's web-site are two of the most frequently visited pages. We estimate that 95% of the visits to the site include use of these tools. Additionally, the program encourages participants to begin thinking about pensionizing a portion of their account balance years before they need to make a firm decision. Over 50% of all quote activity is driven by participants between the ages of 55-65, while 78% of the purchase activity is by participants over the age of 61. The combination of easy to use tools, unbiased education, and low cost delivery can empower individuals to make more financially sound decisions that reflect their personal life circumstances. It is interesting to note that approximately 50% of purchases through the voluntary platform are joint and survivor (J&S). Additionally, this type of platform can be easily integrated with professional assistance or advisory services for participants. Several plan

administrators make service centers available to assist participants with questions and offer assistance as they move through the quote and purchase process. In the setting where participants have access to advisors or assistance with purchases, the percentage of people who choose inflation protected products increases substantially. We believe including objective guidance to participants will improve the take up rate of lifetime income arrangements, but first plan sponsors must feel free to provide access to and promote consideration of lifetime income arrangements without concern over additional liability.

Default options have the potential to be a positive catalyst for change in bringing lifetime income arrangements to plan participants. Given the persistently low take up rates, allowing for a qualified default option for annuitization seems prudent. Technology can play a key role in facilitating default options. One example to consider is what Hueler refers to as a "diverse annuity." Many fiduciaries and professionals believe diversification is a fundamental step towards mitigating provider concentration risk. Many participants express similar concerns. The basic concept is that participants should not annuitize 100% of their balance at one time or invest 100% of their annuity dollars with one provider.

Using technology, sponsors could offer a fully automated default option designed to facilitate establishment of a pre-determined set of criteria for purchasing individual annuities for participants. (i.e. state guarantee fund limits, total dollar amount per contract, or a percentage of total premiums) They may also want to consider the recent survey results from EBRI where 38% of participants favored being required to use $100,000 of their account to purchase lifetime income or 50% percent whichever is less[3]. Once the plan sponsor sets the criteria for diversification, the purchase system would automatically process participants as they were defaulted. The system would calculate the appropriate premium amount to be used for an individual purchase, request a diversified quote across multiple issuers, select the winning quotes starting with the highest income amount, present the monthly payment amount to the participant, and notify parties of the pending withdrawal. This automated default option attempts to address common concerns about concentrating participant retirement savings with one provider and concerns related to offering a single issuer solution that may produce a less than competitive outcome for participants.

Another example where technology could improve delivery is in facilitating the concept of trial annuitization on an automated basis. Trial annuitization may be very appealing to some participants due to the desirable liquidity feature, but others may need or want to maximize their current income amount, which can best be achieved with a lifetime income quote. By automating the process, each participant would always see two quote options. The first quote would reflect a trial annuity that offers enhanced liquidity with a lower monthly income amount. The second quote would offer a monthly lifetime income quote that provides less liquidity but higher monthly income. If the participant did not provide a response, the system would automatically default them into the more liquid trial annuity and if competition is available in this product type, the system could initiate the same diverse annuity quote process outlined above.

## Summary

Receiving lifetime income payments from converted retirement savings that provide a reliable level of financial certainty and reduce very real risks, will promote better financial outcomes and enhance the quality of life for millions of Americans. In order for this to happen, plan participants must be given access to low cost, transparent, annuitization and lifetime income options through an institutional framework. In addition, plan sponsors need a safe harbor that reflects the complexity of today's financial environment relative to issuer selection and they must be encouraged to provide the critical education needed as part of the process. Finally, technology is vital to holding down cost and offering broad based access to lifetime income options.

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**Kelli H. Hueler Biography**
Kelli Hueler is CEO and founder of Hueler Companies, an independent data and research firm providing reporting and systems designed for the annuity and stable value marketplace. Hueler Companies was founded in 1987 and today the firm's data, market research, and analytical reporting are considered the industry standard.

Under Ms. Hueler's leadership, the company developed and launched Income Solutions®; a ground breaking annuity purchase platform. The platform was designed to empower transitioning employees in need of creating a personal lifetime income stream by providing on-line access to competitively bid, institutionally priced annuities. Today the Income Solutions® program is the leading model of its kind for delivery of lifetime income annuities to retirees. The program has been adopted by some of the industry's leading plan administrators and plan sponsors.

Ms. Hueler is nationally recognized as a key contributor on the topic of lifetime income creation. She has testified before the DOL ERISA Advisory Council on annuitization at the point of retirement, presented at the Wharton Pension Research Council, and was tapped to participate in the National Endowment of Financial Education's think tank on income sufficiency. Ms. Hueler presented at the Employee Benefit Research Institutes' National Forum on retirement income sufficiency and at the AARP's "Divided We Fail" initiative in Washington DC. She is a founding member of the DCIIA (Defined Contribution Institutional Investment Association) serving on the Retirement Income Committee and also participates on the Society of Actuaries Committee on Post-Retirement Needs and Risks.

Along with being recognized as a forward thinker in the retirement income arena, Ms. Hueler is also an industry expert in the field of stable value investments. In 2009 she testified before the DOL ERISA Advisory Council regarding Stable Value Funds and Retirement Security in the Current Economic Conditions. She has authored and appeared in numerous articles and spoken internationally on the topic. Ms. Hueler has appeared on investment programs such as *CNN News, CBS' Wall Street Journal Report*. She served on the Board of Directors for the Stable Value Investment Association (SVIA) for six years and additionally served on the SVIA Executive Committee chairing the association's Communication and Education Committee. During Ms. Hueler's tenure, she has also authored chapters for both *"The Handbook of Stable Value Investments"* by Frank Fabozzi and *"Guaranteed Investment Contracts-Risk Analysis and Portfolio Strategies-Edition 2"* by Kenneth L. Walker.

Prior to founding Hueler Companies, Ms. Hueler held the role of Registered Representative for Kidder Peabody & Company and IDS Life where she was responsible for institutional and retail clients. She holds a B.A. from St. Olaf College.