

Financial Engines

Senate Special Committee on Aging

Challenges Women Face in Achieving Retirement Security Hearing Testimony

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Introduction

I would like to thank the Senate Special Committee on Aging for this opportunity to provide testimony. My name is Kelly O'Donnell, and I am a vice president at Financial Engines.

Co-founded in 1996 by Nobel Prize-winning economist Bill Sharpe, Financial Engines works with America's leading employers and retirement plan providers to make retirement help available to approximately 8 million 401(k) participants.¹ Financial Engines is the largest, independent Registered Investment Advisor (RIA) in America.² We are not a fund manager nor do we offer any investment products. We are an independent provider of online advice and discretionary asset management services. Our newest offering, Income+, helps turn a retiree's 401(k) into flexible but steady payouts that can last for life.³ The median account balance we manage is \$41,000.⁴

Women and retirement security is a very personal topic for me. My father unexpectedly passed away last November and helping my mother plan for steady income for the rest of her life is complex and challenging even for a financial professional like myself.

In my testimony today, I will focus on three key points:

First, helping individuals, especially women, maximize their income in retirement, is imperative.

For most individuals, it is hard enough to save and invest in the years before retirement. It is even more difficult to know how to invest and drawdown the assets so one doesn't run out of money in retirement.

Employers are slowly beginning to offer retirement income solutions within 401(k) plans to help participants with this challenge. The income solutions available through employers today include a range of products and services including annuities as well as managed account services such as Financial Engines' Income+. Exhibit 1 provides an overview of the solutions available today as well as the utilization.

While Financial Engines developed Income+ to help all individuals, we find the biggest need is among women. Not only are life expectancies longer for women, but, due to lower salaries or absences from the workplace, women typically have accumulated much less when they reach

¹ As of 3/31/2012.

² InvestmentNews, November 2011.

³ Lifetime income guarantee requires purchase of out-of-plan annuity.

⁴ As of 3/31/2012.

retirement age. Among our clients, the median 401(k) account balance for men age 60 and older is \$82,000 and only \$46,000 for women age 60 and older.⁵

Clearly more needs to be done to help women. For those with low account balances, solutions that merely annuitize retirement accounts will not be sufficient.

My second point is that for women the financial impact from optimal Social Security decisions can exceed 401(k) savings.

Social Security, when claiming is maximized, can significantly increase the amount of income women, particularly married women, are likely to have in retirement.⁶

Women uniquely benefit from good Social Security decisions. For unmarried individuals, the benefit from Social Security deferral depends on life expectancy. Since life expectancy for women is substantially greater than for men, women have the opportunity to get substantial benefits from deferral.

For married women, optimal household strategies for claiming Social Security generally result in a much higher benefit for a surviving spouse, in some cases 76% higher.⁷ Since a surviving spouse is much more likely to be a woman, maximizing this income plays a major role in creating income security for women.

Based on our analyses, optimal Social Security decisions, especially for married women with low balances, can create more retirement income wealth than the woman has accumulated in her 401(k).⁸

My last point is getting the most out of Social Security is often the best way to make a big impact with a small 401(k). However, for women to realize these benefits, they need help. Employer involvement is critical.

The challenges in getting individuals to defer Social Security are formidable. There are both awareness and behavioral challenges. Americans view starting Social Security not as a strategy, but simply something you do upon retirement. And, it's complicated. Determining an optimal strategy depends on marital status, the relative size of each person's earned benefit, interest rates, and life expectancy.

⁵ As of July 2012, Financial Engines Data Warehouse.

⁶ Shoven and Slavaov, The Decision to Delay Social Security Benefits: Theory and Evidence. NBER Working Paper 17866. 2012.

⁷ A claim at 62 results in a benefit amount equal to 75% of the full retirement benefit (FRB). Delaying to age 70 results in a benefit of 132% of the FRB, or a 76% gain.

⁸ Financial Engines Retiree Research Center, 2012.

For many, we believe the best use of retirement accounts is as a bridge to fund retirement in the early years, allowing the deferral of Social Security benefits for as long as possible. I have been involved in testing with employers and participants the concept of applying Income+ so that 401(k) payouts are high in the early years of retirement while Social Security is being deferred. We are very encouraged at the reaction we are getting from both. I believe the challenges in getting someone to defer Social Security can be overcome if they are provided with a plan on how to optimize Social Security and with how to use their 401(k) or IRA as a bridge.

Employers are crucial to bringing this type of help to the broadest number. Aside from Social Security, defined contribution (DC) plans represent the largest source of potential retirement income for millions of American workers. The scale economics of DC plans make it possible for all participants to benefit from institutionally-priced investment products and advisory help. Moreover, the fiduciary role that plan sponsors play is instrumental in making sure participant interests are protected.

In conclusion, we urge more be done to encourage employers to provide retirement income help including help with Social Security strategies for their employees. Every day tens of thousands of Boomers retire, more than half of whom are women. Most of those over 62 start taking Social Security within two months of leaving the workforce, a decision that is irrevocable. Women stand the most to gain by better Social Security decisions and help with maximizing their retirement accounts.

I would like to once again thank the Special Committee on Aging for this opportunity to provide testimony.

Exhibit 1

Retirement Income Solutions and Annuities - Help Offered in 401(k) Plans*

| Plans Already Offer | Retirement Income Solutions |
|---------------------|---|
| 71% | Online modeling tools to help participants determine how much they can spend each year in retirement |
| 42% | Distribution from plan/automatic payment (participant elects an automatic payment from the plan over an extended period of time) |
| 11% | In plan; annuity or insurance products (e.g., variable annuity features, guaranteed minimum withdrawal benefits, preservation of principal, minimum annuity payout, other) |
| 10% | In plan; managed accounts with drawdown features (managed account provider allocates participant assets as well as manages the amount paid each year from the plan) |
| 10% | In plan; managed payout funds (funds with an allocation targeted at a specific payout percentage each year with no guarantees) |
| 9% | Facilitation of annuities outside the plan as options for plan distributions |
| 6% | Ability to transfer assets to a Defined Benefit plan in order to receive an annuity |

*Source: Aon Hewitt, [2012 Hot Topics in Retirement](#).

