PRESIDENT'S ADVISORY
PANEL
ON FEDERAL TAX REFORM

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Response to April 5, 2005, Request for Public Comment by the President's Advisory Panel on Federal Tax Reform

Submitted by

Joseph F. McKeever, III

on behalf of the

Committee of Annuity Insurers

(Category of submitter: Organizations and Associations)

April 28, 2005

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April 28, 2005

VIA FIRST CLASS MAIL

The President's Advisory Panel on Federal Tax Reform
1440 New York Avenue, NW
Suite 2100
Washington, DC 20220

Re: Committee of Annuity Insurers Response to April 5, 2005, Request for Comments by the President's Advisory Panel on Federal Tax Reform

Dear Sir or Madam:

I am writing on behalf of the Committee of Annuity Insurers (the "Committee") in response to the April 5, 2005, press release by the President's Advisory Panel on Federal Tax Reform (the "Panel"), in which the Panel invited interested parties to submit ideas for reforming the federal tax code. The Committee is a coalition of 29 of the nation's largest and most prominent issuers of annuity contracts, representing more than half of the annuity business in the United States.[1] As discussed in more detail below, the Committee urges the Panel to consider a specific reform to the current tax code that would facilitate a more secure retirement for Americans by encouraging them to utilize annuities that provide a retirement income stream that is guaranteed to last throughout their lifetimes.

[1] The Committee was formed in 1982 to address federal legislative and regulatory issues relevant to the annuity industry and to participate in the development of federal policy regarding annuity taxation. A list of the member companies is attached.

The Panel's recent request for public comment reiterated the President's directive that the Panel's proposals for tax reform should "promote long-run economic growth and job creation, and better encourage work effort, saving, and investment . . ." In this regard, as the Committee described in its March 17, 2005, letter to the Panel, long-run economic growth and job creation are fostered when Americans are encouraged to save, and in fact do save, for their retirement years,[2] and thus it is important that the tax code continue to encourage retirement savings. But *accumulating* sufficient savings is not enough. Americans also need the ability to make their accumulated savings *last throughout their retirement*.

As a result of increases in life expectancy and other factors,[3] Americans are spending a greater proportion 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.[4] In addition, the 70-million-strong baby boom generation is approaching retirement, which means that many more Americans will soon need retirement income to support their basic needs and maintain a comfortable standard of living.

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[2] Numerous studies make this point, but of particular interest here is M. BOSKIN, B. BERNHEIM, AND P. BAYER, THE ECONOMIC ROLE OF ANNUITIES (Catalyst Institute, March 1998) (available at www.annuity-insurers.org).

[3] In the early 1900's, life expectancies at birth were 58.3 years for females and 51.5 years for males. A century later, those figures are 84 years for females and 80 years for males, and most demographers predict continued increases in life expectancy going forward. Jeffrey R. Brown, *The New Retirement Challenge* (September 2004).

[4] *Id.*

Other than Social Security and employer-sponsored defined benefit plans, annuities are the only means that Americans have to *guarantee* they will not outlive their retirement income.[5] This type of guarantee is becoming increasingly important in light of factors such as reduced coverage by employer-sponsored defined benefit plans and the limited amount of pre-retirement income that typically is replaced by Social Security. Absent such guaranteed retirement income, many Americans may run out of savings or face very difficult circumstances. On the other hand, retirees who receive guaranteed lifetime income from products like annuities can be expected to have an adequate standard of living, even if they live into their 90s or beyond; live more independently (and avoid becoming a burden on others); and have the peace of mind that guaranteed lifetime income can bring. To promote these and other societal benefits of guaranteed retirement income streams, the tax code should include incentives that encourage Americans to choose life-contingent annuity payments.

In this regard, the Committee urges the Panel to consider reforms to the existing tax code that would include such incentives. Legislation that would accomplish this goal already has been introduced in both Houses of Congress. The Retirement Security for Life Act (H.R. 819 and S. 381) would provide an exclusion from income for up to 50% of the portion of life-contingent annuity payments that are otherwise taxable under the current tax code. The most that could be excluded from income in any one year under the bill would be $20,000.[6] The 50%

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[5] *See, generally,* J. BROWN, O. MITCHELL, J. POTERBA, AND M. WARSHAWSKY, THE ROLE OF ANNUITY MARKETS IN FINANCING RETIREMENT (MIT Press, 2001).

[6] Thus, for example, a person in the 15% tax bracket could receive an annual tax benefit of up to $3,000.

exclusion and $20,000 dollar cap were carefully chosen to ensure that the bill will provide a meaningful economic incentive for Americans to choose life-contingent retirement income streams that can help them ensure a secure retirement, while at the same time limiting the revenue costs of the proposal.[7]

The bill's income tax exclusion would be available only for annuities purchased with after-tax personal savings and only for payment streams from such annuities that are guaranteed to last the entire life of the retiree (or joint lives of the retiree and his or her spouse). Such annuities can be commercially issued only by life insurance companies, which are subject to a comprehensive state regulatory regime designed to assures that the benefits promised to annuitants will be provided.

The bill would accomplish the foregoing by a simple supplement to the provisions of the current tax code that govern how the taxable portion of annuity payments is calculated.[8] The existing provisions would continue to operate as under current law, and the bill's 50% income tax exclusion then would be applied after the current-law calculation. These changes to the tax code would not result in any significant increase in administrative or compliance costs.

The Committee strongly supports the Retirement Security for Life Act, and believes that it provides an ideal solution to the societal problem of ensuring adequate income for Americans throughout their retirement. This problem has become more acute in recent years due

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[7] The Joint Committee on Taxation has not provided a revenue estimate of the proposal.

[8] Under current law, a portion of annuity payments received in a year is treated as a return of the after-tax dollars the taxpayer used to purchase the product (and, thus, is not taxed again), while the remaining portion is taxable at ordinary income tax rates. *See* IRC section 72(b).

to factors such as earlier retirements, advances in medical technology and increases in life expectancies, declines in traditional defined benefit pension coverage, limited income replacement by Social Security, and the pending retirement of the baby boom generation. By encouraging Americans to convert a portion of their accumulated savings into retirement income streams that cannot be outlived, the tax code would go a long way towards addressing this important issue. Accordingly, the Committee urges the Panel to consider incorporating the proposal embodied by the Retirement Security for Life Act into one or more of the Panel's recommendations.

The Committee appreciates this opportunity to respond to the Panel's invitation for public comment. We continue to offer the Committee's expertise on annuities and retirement security as a resource to the Panel and would look forward to providing any assistance that the Panel believes would help in meeting its important objectives.

Sincerely,

Joseph F. McKeever, III

Attachment

The Committee of Annuity Insurers
The Willard Office Building
Suite 1200
1455 Pennsylvania Ave., NW
Washington, D.C. 20004

Allmerica Financial Company, Worcester, MA
Allstate Financial, Northbrook, IL
American International Group, Inc., Wilmington, DE
AmerUs Annuity Group Co., Topeka, KS
AXA Equitable Life Insurance Company, New York, NY
F & G Life Insurance, Baltimore, MD
Fidelity Investments Life Insurance Company, Boston, MA
Genworth Financial, Richmond, VA
Great American Life Insurance Co., Cincinnati, OH
Guardian Insurance & Annuity Co., Inc, New York, NY
Hartford Life Insurance Company, Hartford, CT
ING North America Insurance Corporation, Atlanta, GA
Jackson National Life Insurance Company, Lansing, MI
John Hancock Life Insurance Company, Boston, MA
Life Insurance Company of the Southwest, Dallas, TX
Lincoln Financial Group, Fort Wayne, IN
Merrill Lynch Life Insurance Company, Princeton, NJ
Metropolitan Life Insurance Company, New York, NY
Nationwide Life Insurance Companies, Columbus, OH
New York Life Insurance Company, New York, NY
Northwestern Mutual Life Insurance Company, Milwaukee, WI
Ohio National Financial Services, Cincinnati, OH
Pacific Life Insurance Company, Newport Beach, CA
The Phoenix Life Insurance Company, Hartford, CT
Protective Life Insurance Company, Birmingham, AL
Prudential Insurance Company of America, Newark, NJ
Sun Life of Canada, Wellesley Hills, MA
Travelers Insurance Companies, Hartford, CT
USAA Life Insurance Company, San Antonio, TX

The Committee of Annuity Insurers was formed in 1982 to participate in the development of federal tax policy with respect to annuities. The member companies of the Committee represent over half of the annuity business in the United States.