TRANSAMERICA®
Stable Value Solutions

TRANSAMERICA STABLE VALUE TELEGRAPH

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A Wrapper's View on Underwriting
by Nicole Plourde

How a wrapper underwrites a plan may seem like a mystery to others.

For Transamerica Stable Value Solutions, the underwriting process plays an important role as a jumping off point for many business decisions. Therefore, we decided to give you a little sneak peek into our "black box" so you, as a manager or plan sponsor, can better understand some of the factors underlying many of our decisions.

When underwriting a plan, we focus on three things: the plan participants, the plan itself, and the plan sponsor. The criteria relating to plan participants are most heavily weighted, making up over half the weighting, while the criterion concerning the sponsor is the least weighted. The underwriting looks solely to plan characteristics, not portfolio characteristics. However, it should be noted that when making a final business decision, we do take into account many other factors (e.g., market-to-book ratio, crediting rate, buffer, timing, etc.).

To dive into things a little deeper, when looking at participant-related criteria, we are more specifically looking at cash flows and demographics. When we look at cash flows, the longevity and stability of the fund are highly important. We analyze how contributions compare to distributions and the extent to which one outweighs the other. We also analyze the trends of contributions, distributions, and transfers. For us, having a full understanding of what is driving cash flows is a crucial aspect of the underwriting, which naturally brings us next to demographics. With regard to demographics, we are concerned about both current and future withdrawal pressure. Therefore, we evaluate both inactive and active participant balances.

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In This Issue

The Fiscal Cliff
by Dave Halfpap and Frank Rybinski

INTRODUCTION—On January 1, 2013, a combination of spending cuts and tax increases will take hold that impacts virtually everyone and threatens to throw the U.S. economy into a serious nosedive. With each passing day the U.S. economy draws nearer to the impending fiscal tightening of numerous tax breaks currently on the books, along with various new policies increasing taxes and cutting government spending. Virtually all economic models suggest the current law will severely

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What Matters Most

A survey commissioned by the Transamerica Center for Retirement Studies® highlights American workers' priorities for the President and Congress regarding retirement security.

As part of its 13th Annual Transamerica Retirement Survey, the Transamerica Center for Retirement Studies® (the "Center") asked American workers: "With the November 2012 election in mind, which of the following should be priorities for the next President and Congress to help Americans prepare for a financially secure retirement?" The Center published results to raise awareness of the issues and the important role of policymakers in helping Americans achieve retirement readiness.

More than half of the 3,609 survey respondents – 57 percent – think that fully funding Social Security to ensure that all Americans receive their guaranteed benefits should be a priority. Other popular responses relate to providing tax credits for workers who make contributions to an individual retirement account (IRA), a 401(k) or similar plan, as well as implementing financial literacy courses in schools to teach Americans how to save for retirement.

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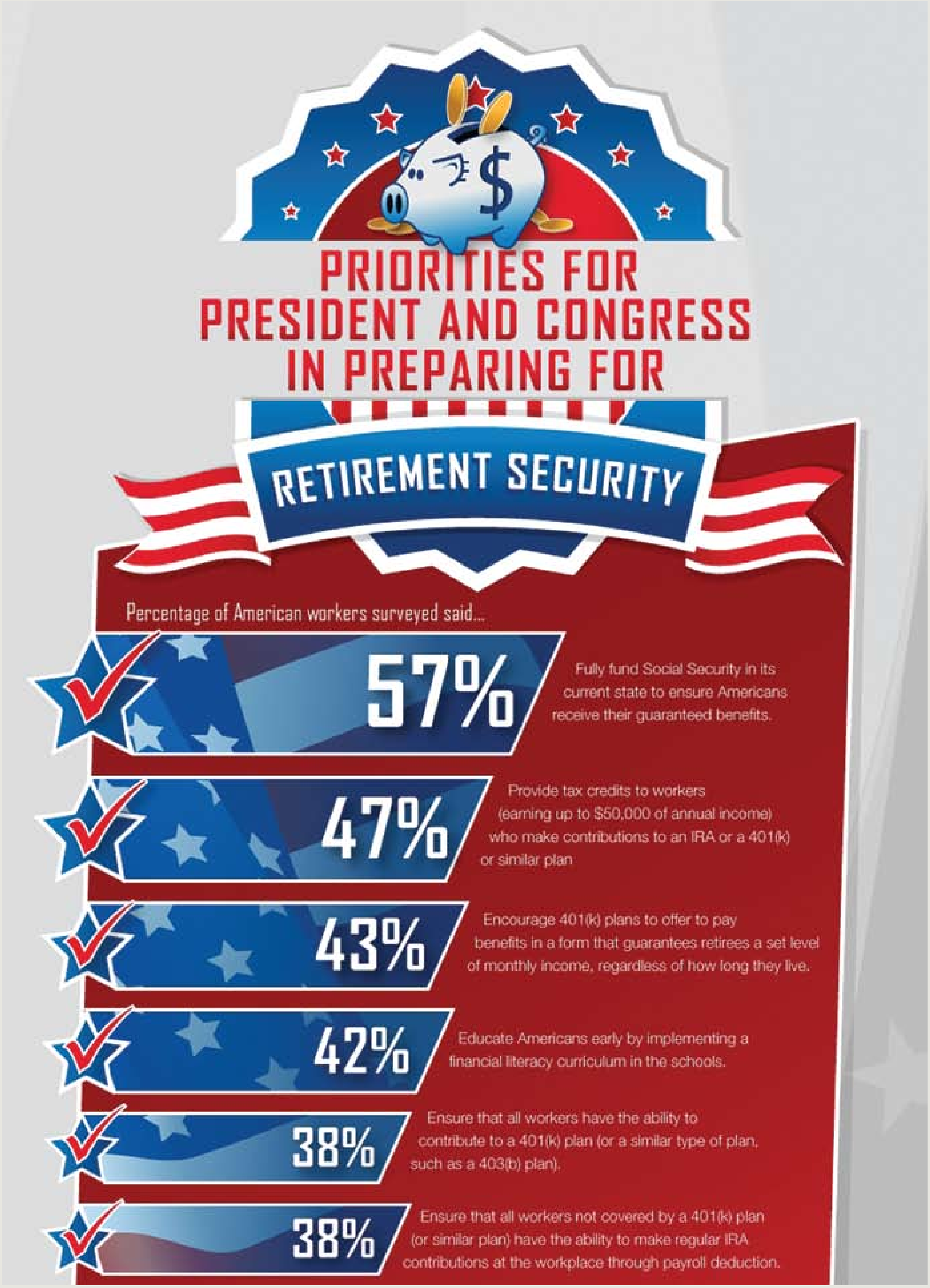
The Transamerica Center for Retirement Studies® is a non-profit, private foundation and is funded by contributions from Transamerica Life Insurance Company and its affiliates and may receive funds from unaffiliated third parties. This survey was conducted online within the U.S. by Harris Interactive on behalf of TCRS between 1/13/12 – 1/31/12 among 3,609 full-time and part-time workers. Potential respondents were targeted based on job title and full-time and part-time status. Respondents met the following criteria: U.S. residents, age 18 or older, full-time or part-time workers in for-profit companies, and employer size of 10 or more. For more information about TCRS, please refer to www.transamericacenter.org or send an email to info@transamericacenter.org. TCRS and its representatives cannot give ERISA, tax, investment or legal advice.

A Wrapper's View, cont. from page 1

As an extension of our analysis of participant cash flows, we evaluate the plan options. Other funds and options offered by the plan can intensify the risk of transfers. We look into competing funds and self-directed brokerage windows to evaluate usage percentages as well as whether equity washes are in place. Asset allocation models are also taken into account. Although we have generally been comfortable with advice models, we are less comfortable with managed accounts and therefore have developed business terms to mitigate the risk associated with such programs.

Lastly, we assess the plan sponsor. Although there is no sure-fire way to know if an employer may initiate actions that could have a detrimental effect on the stable value fund, we do look at the credit quality of the plan sponsor. We use credit quality as a proxy for the health of the company. For private companies, states, and municipalities without credit ratings, we have developed alternative methods to review the financial health of the sponsoring entity.

The underwriting process for Transamerica goes beyond just the initial plan review that occurs when we enter into a new contract. Not only do we re-underwrite each plan and pool on an annual basis, we update the underwriting in conjunction with large plan changes or unusual changes to the wrap transaction flow, or when a significant news event affects the company. Given the significance of plan underwriting in our business decision process, we wanted to give you a better understanding of what we focus on when underwriting a plan and hope this summary brings clarity to a process that can seem somewhat mysterious.


PRIORITIES FOR PRESIDENT AND CONGRESS IN PREPARING FOR
RETIREMENT SECURITY
Percentage of American workers surveyed said...
57%
Fully fund Social Security in its current state to ensure Americans receive their guaranteed benefits.
47%
Provide tax credits to workers (earning up to $50,000 of annual income) who make contributions to an IRA or a 401(k) or similar plan
43%
Encourage 401(k) plans to offer to pay benefits in a form that guarantees retirees a set level of monthly income, regardless of how long they live.
42%
Educate Americans early by implementing a financial literacy curriculum in the schools.
38%
Ensure that all workers have the ability to contribute to a 401(k) plan (or a similar type of plan, such as a 403(b) plan).
38%
Ensure that all workers not covered by a 401(k) plan (or similar plan) have the ability to make regular IRA contributions at the workplace through payroll deduction.

The Fiscal Cliff, cont. from page 1

impact the U.S. economy, most likely tipping it toward recession. The purpose of this article is to explore in some depth the detail around the legislative changes and how one should look at this current risk from an investment strategy standpoint.

What is the Fiscal Cliff?

Depending on one's estimates, the aggregate dollar amount of the fiscal cliff is between $600 - $750 billion (equivalent to 3.5% - 5% of GDP), with two-thirds coming from changes in taxation and one-third from spending cuts. Below and to the right are tables showing the changes brought on by the current law set to take effect on the 1st of January. Note the new policies in place, the additional taxation from the Affordable Care Act and the automatic spending cuts also scheduled for January 1st.

The next two tables put some context around what exactly the new policies would target.

2013 Current Law	Change, YoY (in $ Billions)	% GPD '13
Expiring Policies		
Payroll Tax Cut	125	0.8%
Partial Bush Tax Cuts - Upper Class	100	0.6%
Partial Bush Tax Cuts - Middle Class	150	0.9%
AMT Patch	50	0.3%
Jobless Benefits	35	0.2%
Other	200	1.2%
Total Expiring Policies	660	4.0%
New Policies		
Affordable Care Act (ACA)	45	0.3%
Spending Sequestration	85	0.5%
Total New Policies	130	0.8%
TOTAL FISCAL DRAG	790	4.8%

Source: CBO, Deutsche Bank

2013 Current Law	Description of Policy Implication
Individual Tax Brackets	The Bush tax cuts from 2000 expire
	Top Rate: 35% -> 39.6%
	Middle Rates all 3 percentage points higher
	Eliminate 10% rate
Other Tax Changes	Payroll tax 'Holiday' expires: Social Security tax 4.2% -> 6.2%
	No AMT indexing - over 30 million individuals become eligible to pay
	Higher Estate Tax
	Higher Marriage Penalty
	Itemized deductions phase out
	Tax credits reduced/eliminated (child, adoption, dependent care)
Penalize Savings	Long Term Capital Gains Increase: 15% -> 20%
	Dividends were taxed at 15%, now to be taxed as ordinary income.
Healthcare Tax	New investment income tax of 3.8%
	Additional health insurance tax of 0.9% on high income earners.
Corporations	Changes to depreciation schedules
Spending Sequestration	Automatic spending cuts commence per the Budget Control Act. Lawmakers set discretionary spending caps which, when fully implimented, are scheduled to save $900 billion by 2021. (Entitlements and Retirement Funds not affected.)
Unemployment Benefits	Reduction in number of eligible weeks

Source: CBO, Credit Suisse, Citi Research

1) There is a change in the intrinsic incentive structure of the U.S. economy. Specifically, work and saving will be taxed more – the latter is not as palatable given how low the nation's historical savings rate has been, particularly when coupled with the secular budget-busting issue of social security, which is not addressed in this legislation.

2) Take the pain now or later: With regards to the fiscal cliff, this refers to the tradeoff between (1) taking the pain up front and forcing an immediate recession, or (2) water down the new legislation so much that it hurts the long term credit quality of the U.S. government by exacerbating the national debt (Moody's has already fired a downgrade shot across the bow in this regard). While there is a relatively safe path in the middle, the current level of political rancor makes getting there all the more onerous.

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When looking at the areas impacted, two things jump out to us:

FEDERAL INCOME TAX BRACKETS

SINGLE FILERS

Income Level ($)		Current Law		
Over	Up To	'12 Rate	'13 Rate	Chg ppt
0 -	8,750	10%	15%	5%
8,750 -	35,500	15%	15%	0%
35,500 -	86,000	25%	28%	3%
86,000 -	179,400	28%	31%	3%
179,400 -	199,350	33%	36%	3%
199,350 -	390,050	33%	36%	3%
390,050 -	and up	35%	39.6%	4.6%

Source: Tax Policy Center, Credit Suisse

MARRIED FILING JOINTLY

Income Level ($)		Current Law		
Over	Up To	'12 Rate	'13 Rate	Chg ppt
0 -	17,500	10%	15%	5%
17,500 -	59,300	15%	15%	0%
59,300 -	71,000	15%	28%	13%
71,000 -	143,350	25%	28%	3%
143,350 -	218,450	28%	31%	3%
218,450 -	241,900	33%	36%	3%
241,900 -	390,050	33%	36%	3%
390,050 -	and up	35%	39.6%	4.6%

Historically, a fiscal contraction of the scheduled size would be the largest on record, exceeding the 3% contraction in 1969. Two notables: (1) it was a much better economic environment to enact this magnitude of fiscal contraction as the U.S. economy was on much better footing (it grew +4.8% in real terms), and (2) it still contributed to a recession in 1970. Furthermore, monetary policy is already quite accommodative, so its ability to further offset a 'Full Cliff' contraction would be limited.

Has Washington Gone Mad?

Washington doesn't tend to have a long-term time horizon. Instead it focuses on what's right in front of their nose, and currently it is the election! Why worry about some concern three months from now when we have more pressing matters! Most of the feedback from Washington is they are firmly aware of the Fiscal Cliff and most likely will reach some deal in the lame duck session, to either solve the issue or more likely kick it down the road. But the current state of contentious gridlock on fiscal policy most likely won't go away after the election unless a sweeping mandate unfolds one way or the other. Both sides will claim electoral mandates to stick to their positions, all the while edging closer to the cliff and leading to huge uncertainty in the financial markets. Currently, the consensus of the markets seems to be that cooler heads will ultimately prevail and some type of agreement will be reached to avoid the cliff.

One positive aspect within all of this drama is that another player has entered the fray – the rating agencies. Moody's has been very clear about its intentions to downgrade U.S. debt if Congress is unable to enact some plan to deal with our ongoing debt crisis. Such a plan is what most in Washington refer to as completely revamping the current tax code along with subsequent spending cuts – no easy task, and surely not one that will get done in a lame duck session. The markets appear to be discounting a kick-of-the-can down the road approach, but only a short road, as they eventually expect to see credible progress on a plan that will eventually reduce the growth rate of debt, while at the same time provide incentives for economic growth.

Washington finds itself in a position they are not accustomed to – having the markets dictate their actions. You may recall back in the late summer of 2008 when the first vote was taken to pass the Emergency Economic Stabilization Act (EESA). Congress voted it down only to see the stock market fall several hundred points. A few days later they had collected their senses and passed the legislation. Consider the current dilemma – if we go over the cliff, the U.S. economy will more than likely enter a recession. But even if some compromise is reached they still are not off the hook, as Moody's is still lurking with their potential downgrade. To Moody's credit, they have served up a solution on a silver platter by saying that the budget doesn't need to be balanced immediately, instead they are looking at the slope of the buildup of debt outstanding and want to see that slope falling in the far out years of the budget. The only way that will happen is addressing entitlements and medical spending.

How Does One Prepare for the Cliff?

Handicapping the outcome is extremely difficult, especially given the track record we've experienced over the past several years out of Washington. The Market continues to believe that something will get done, but experience considerable volatility along the path. In the short run everyone knows that to do nothing would be foolhardy and therefore logical heads should prevail, but if they don't, refer back to the EESA enactment of 2008 and the debt ceiling fiasco of 2011. In both instances the market took a severe short-term drubbing only to be higher a year later. If we go over the Cliff or Washington drags its feet on figuring out a long-term

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Picture this: a group of finance geeks who are armed with power tools and aren't afraid to use them. Worse still, they have a jackhammer, a really big jackhammer...

In the House with SVS: A Habitat for Humanity Story

by Kappie Bogart

On May 10th, a team of employees from Transamerica Stable Value Solutions (SVS) spent the day working on two houses in the Baltimore area. They joined other teams across the country from the Employer Solutions & Pensions (ES&P) division of the AEGON U.S. life insurance companies who also volunteered their time during the month of May building homes with Habitat for Humanity and meeting the families who will benefit from the program.

ES&P was the first Transamerica division to partner with Habitat for Humanity International on such a major initiative. More than 450 volunteers worked a total of 25 days at 13 different build sites. These events gave back to their respective communities while also strengthening teamwork and providing opportunities for learning new skills. (For example, I learned how to use a jackhammer, which should serve me well in future contract negotiations.)

In Baltimore, half of the SVS team framed walls and floors in one house while, in the other house, the other half of the team hauled debris and demolished the 6-inch deep concrete basement floor using the aforementioned jackhammer, along with various pick axes and sledgehammers. Despite and perhaps even because of the amount of laughter and unintended silliness that can accompany this type of event (e.g., one team member pinned his finger to the wall with a 2x4), the teams successfully completed their respective jobs and more.

At the end of the day, while there were plenty of sore muscles, there were no injuries and the overwhelming feeling on the team was pride in a job well done. When asked about participating in future Habitat builds, all team members were enthusiastic about the benefits of the build day both to the community and to the team.

An on-site Habitat observer complimented the SVS team on its willingness to do whatever was necessary, no matter how menial. It was clear to all that we took our roles seriously and came to work. SVS has continued to support Habitat by making donations to Habitat on behalf of clients who completed the client satisfaction survey and future build dates are already being contemplated by the group.

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The Fiscal Cliff, cont. from page 5

game plan, take solace from the fact that new players are in the room to finally hold them accountable – the ratings agencies and Mr. Market.

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