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# Filling The Void In Guaranteed Retirement Income

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## Agenda

1. The Retirement Preparedness Problem
2. DC Plan Income Solutions
3. Due Diligence on DC Annuity Solutions
4. Questions and answers

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## The Retirement Preparedness Problem

## Shifting the Burden to Employees

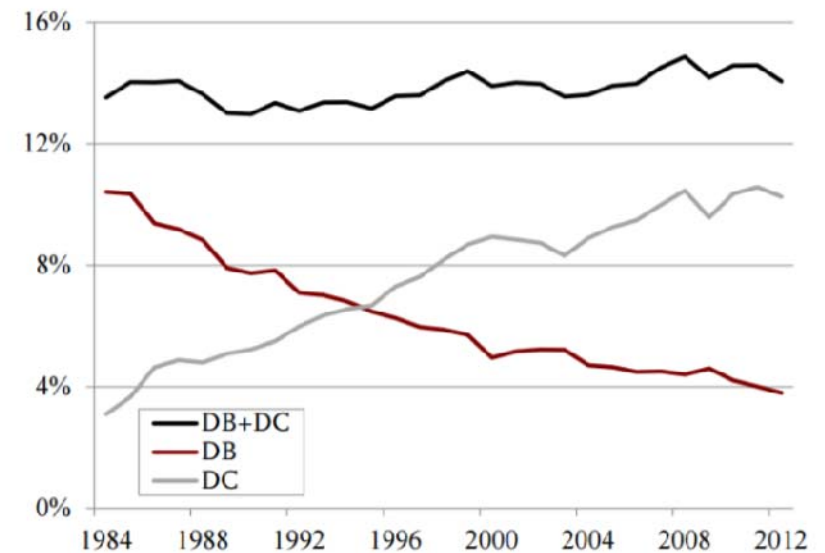
Source:

*HOW HAS SHIFT TO DEFINED CONTRIBUTION PLANS AFFECTED SAVING?*

By Alicia H. Munnell, Jean-Pierre Aubry, and Caroline V. Crawford

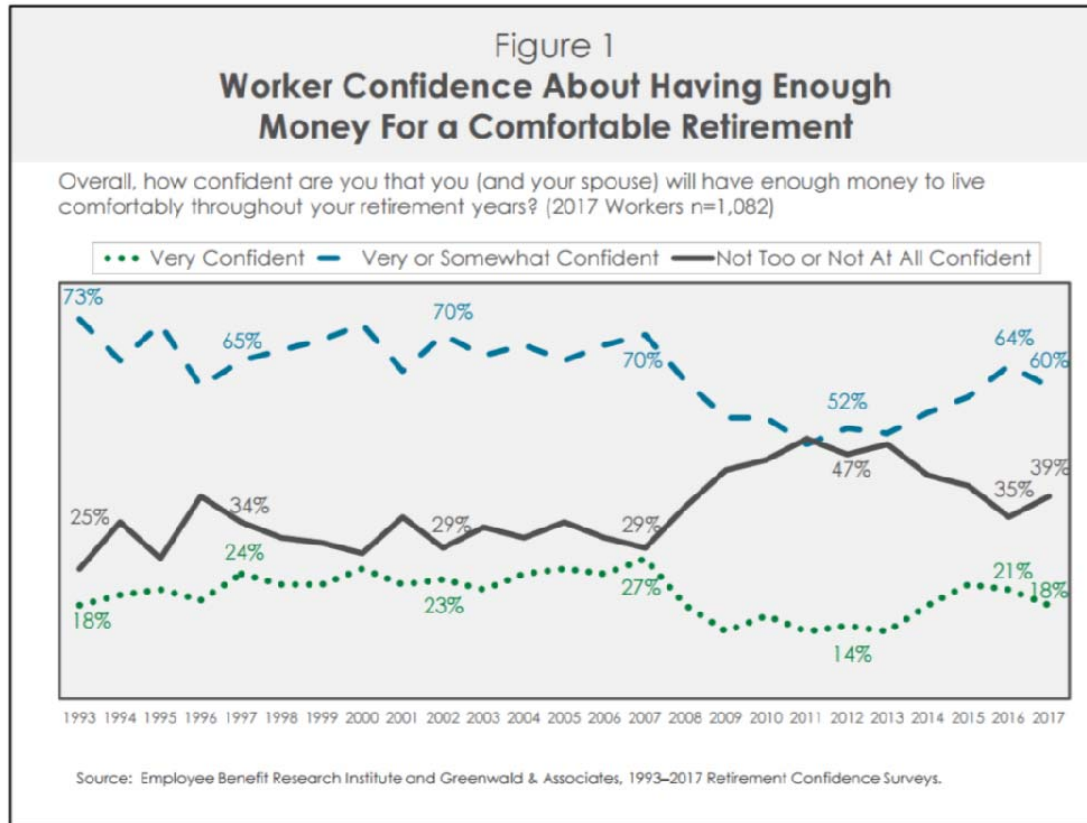
Published by the Center for Retirement Research at Boston College  
September 2015

FIGURE 7. ANNUAL CHANGE IN DB AND DC PENSION WEALTH AS A PERCENTAGE OF PRIVATE WAGES AND SALARIES, 1984-2012



Sources: Authors' calculations from NIPAs (1984-2012); Form 5500 (1989-2012); *Flow of Funds* (2014); and SCF (1989-2013).

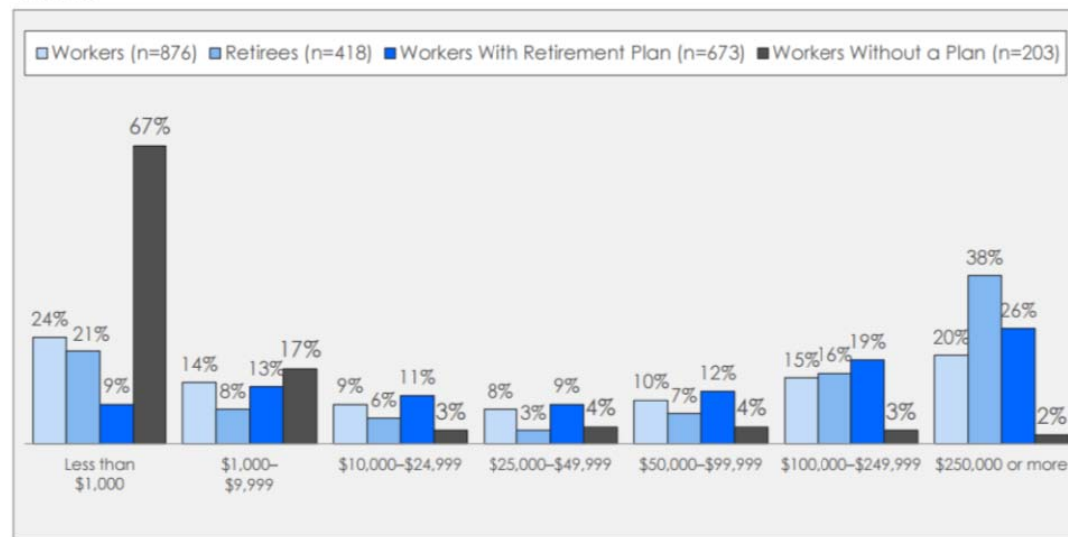
## Feeling Unprepared



## Precarious State of Savings

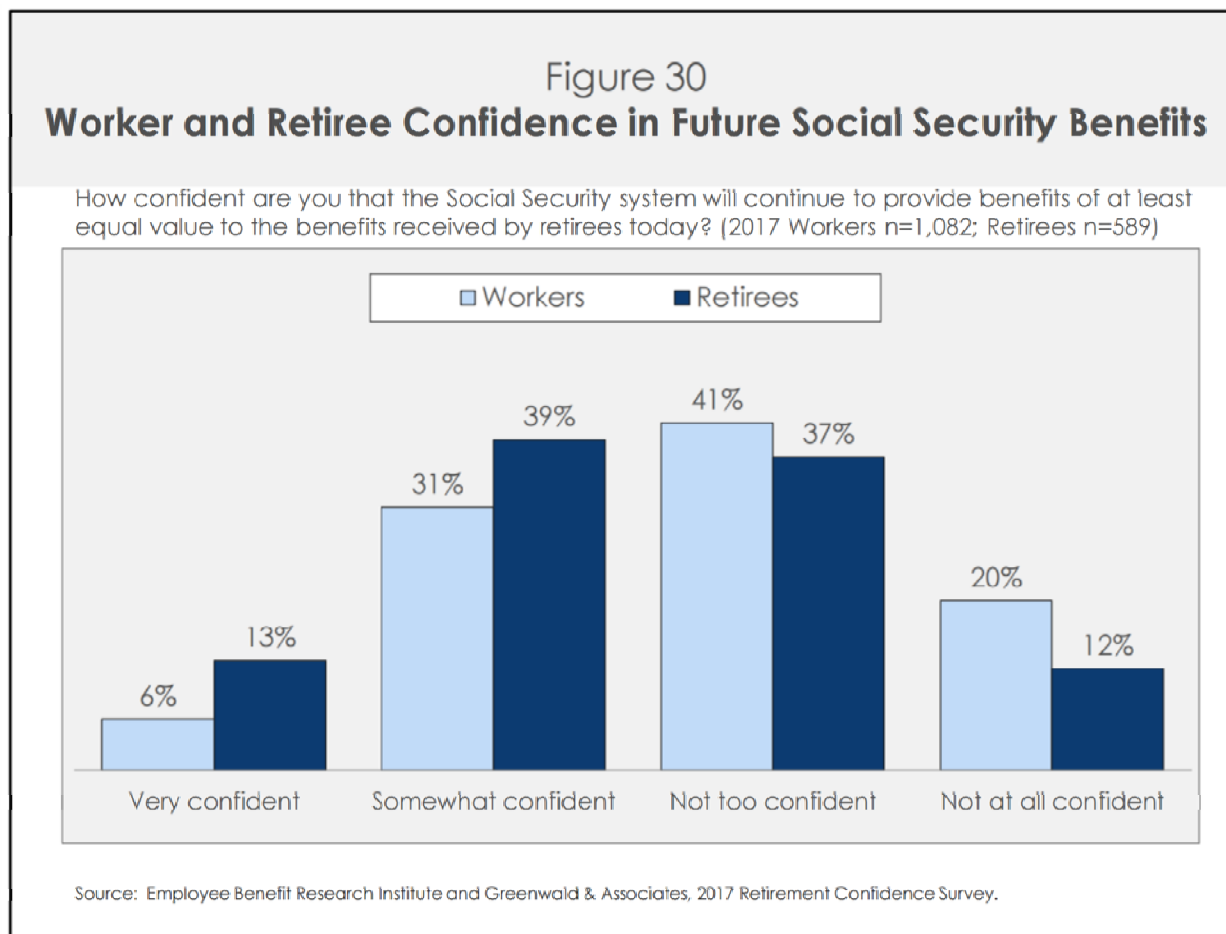
Figure 13  
**Worker and Retiree Savings Amounts, by Plan vs. No Plan**

In total, about how much money would you say you (and your spouse) currently have in savings and investments, not including the value of your primary residence or defined benefit plan assets?



Source: Employee Benefit Research Institute and Greenwald & Associates, 2017 Retirement Confidence Survey. Figures and n-sizes presented exclude those who answered "Don't know," said they never worked, or refused to answer.

## Lack of Confidence in Social Security

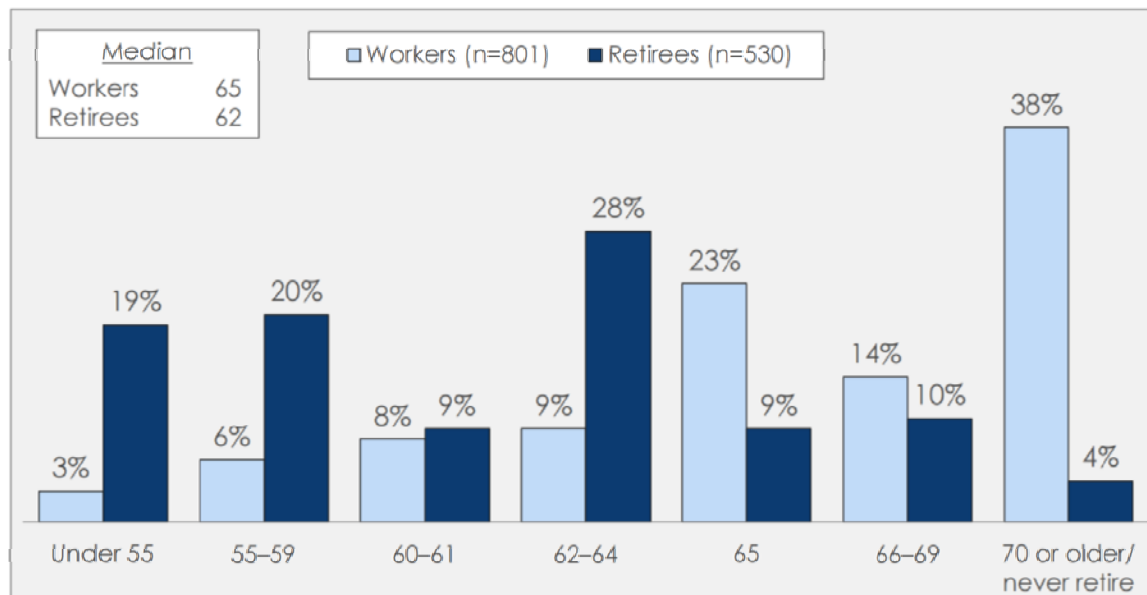




## Employment Insecurity

Figure 26  
**Worker Retirement Age Estimates vs. Retiree Retirement Ages**

Realistically, at what age do you expect to retire?/How old were you when you retired?



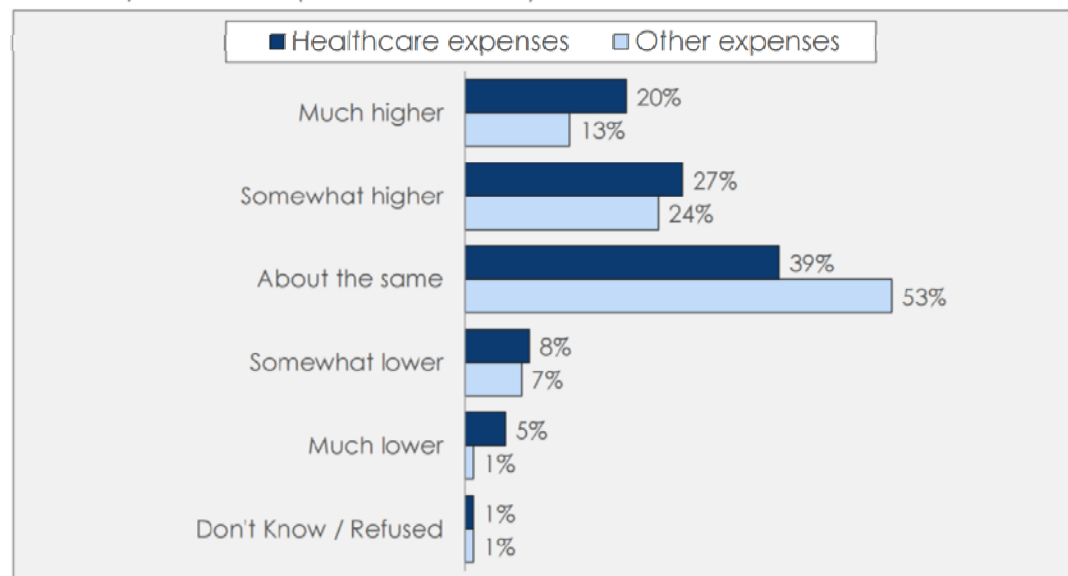
Source: Employee Benefit Research Institute and Greenwald & Associates, 2017 Retirement Confidence Survey. Figures and n-sizes presented exclude those who answered "Don't know," said they never worked, or refused to answer.

## The Real Cost of Living

Figure 34

**Retirees' Actual Expenses in Retirement  
Compared With Their Expectations**

Compared with what you expected when you first retired, would you say your **healthcare expenses/other** in retirement are higher, about the same, or lower than you expected them to be at this point in time? (2017 Retirees n=589)

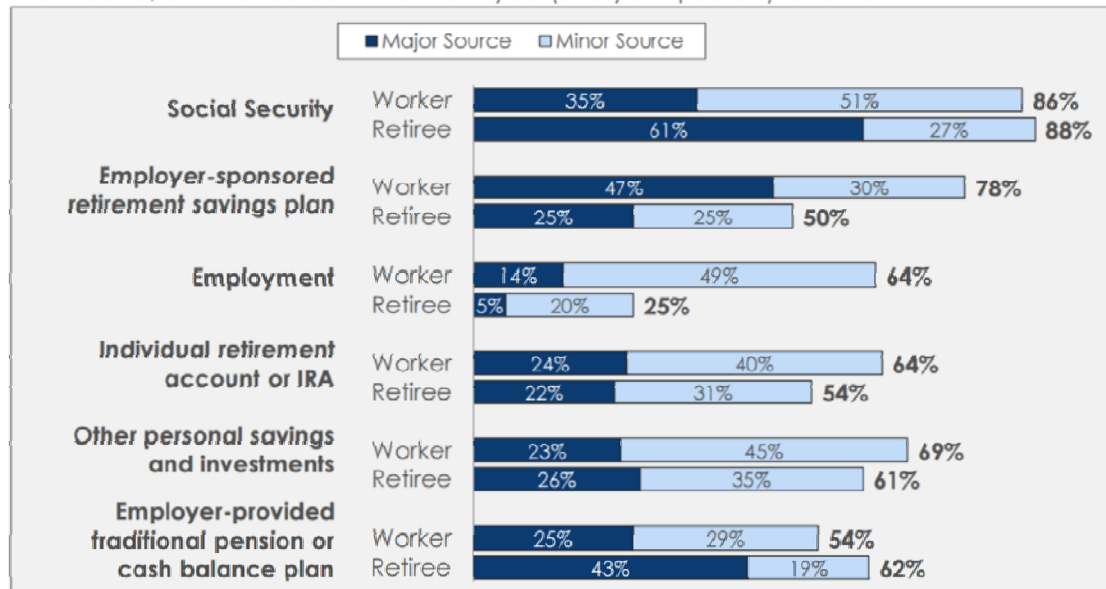


Source: Employee Benefit Research Institute and Greenwald & Associates, 2017 Retirement Confidence Survey.

## Finding a Way

Figure 29  
**Worker Expectations for Sources of Income in Retirement vs. Retirees' Actual Income Sources**

Do you expect the following will be/is the following a major source of income, a minor source of income, or not a source of income in your (and your spouse's) retirement?

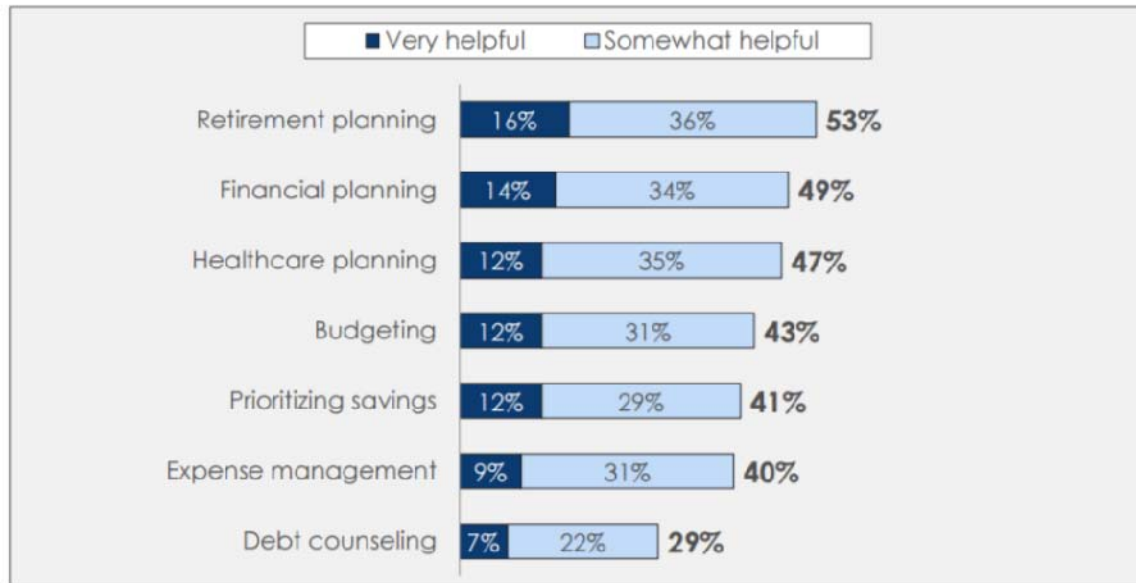


Source: Employee Benefit Research Institute and Greenwald & Associates, 2017 Retirement Confidence Survey.

## Interest in Education

Figure 10  
**Helpfulness of Financial Education Programs  
 in Increasing Productivity at Work**

How helpful, if at all, do you think the following programs would be for increasing **your productivity at work**...? (Employed, Workers n=799)

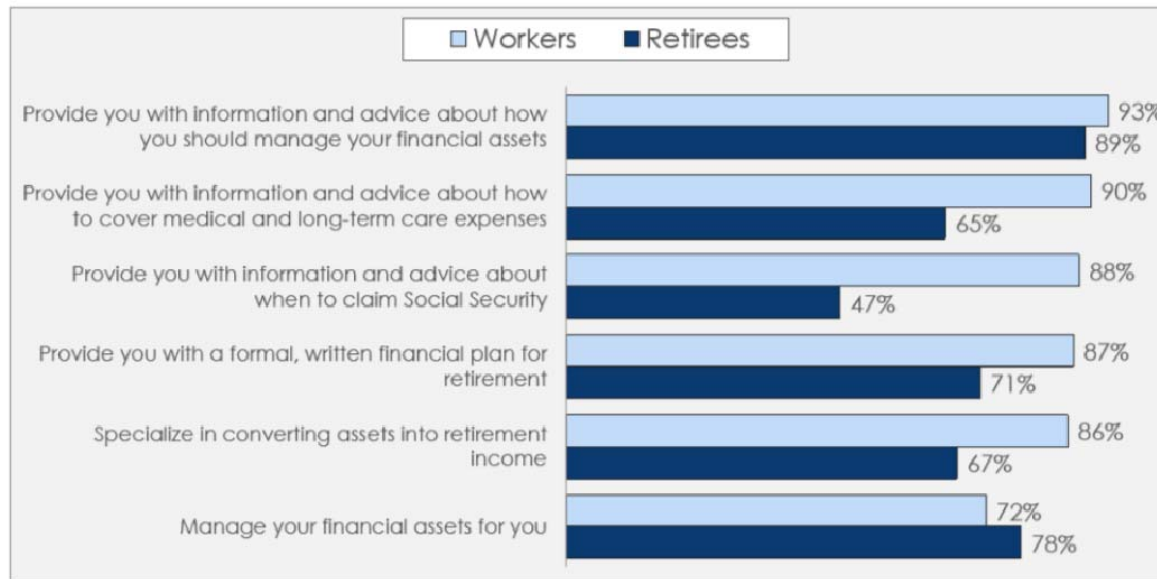


Source: Employee Benefit Research Institute and Greenwald & Associates, 2017 Retirement Confidence Survey.

## Advice Workers Want

Figure 20  
**Important Financial Advisor Characteristics/Services**

How important (will it be/is it) for the adviser you chose to...? (Those who work with or expect to work with a financial adviser, Workers n=546, Retirees n=229, percent very/somewhat important)



Source: Employee Benefit Research Institute and Greenwald & Associates, 2017 Retirement Confidence Survey.

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## The High Cost of Living Longer

Source:

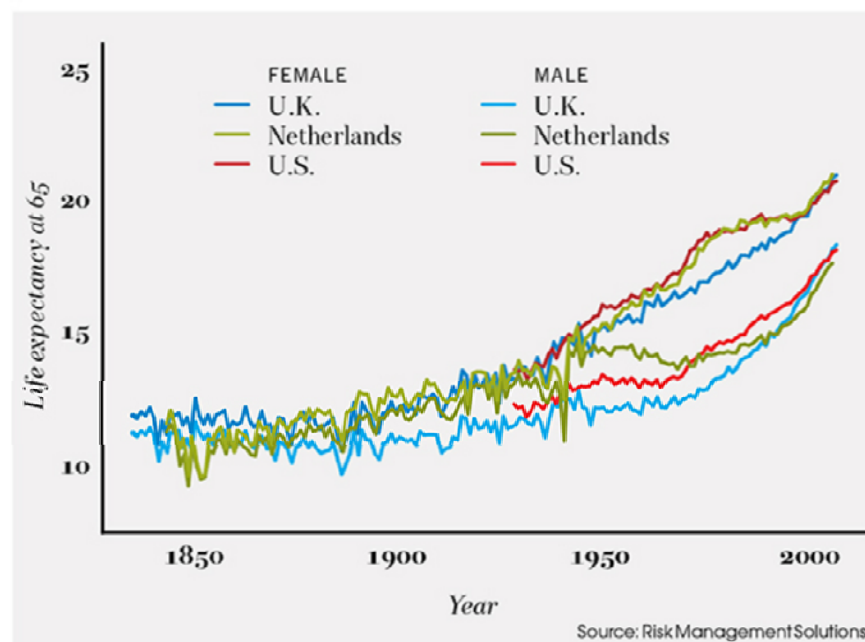
*The Rising Challenge of Measuring and Managing Longevity Risk*

Institutional Investor

August 25, 2014

### Greater expectations

Life expectancy has steadily grown since the early 19th century. Today every additional five years demands \$1 trillion more from defined benefit pension plans.



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## Investment and Lifespan Uncertainty

*“For the typical investment strategy, investment risk is larger at younger retirement ages, but longevity risk becomes larger with time.”*

Source:

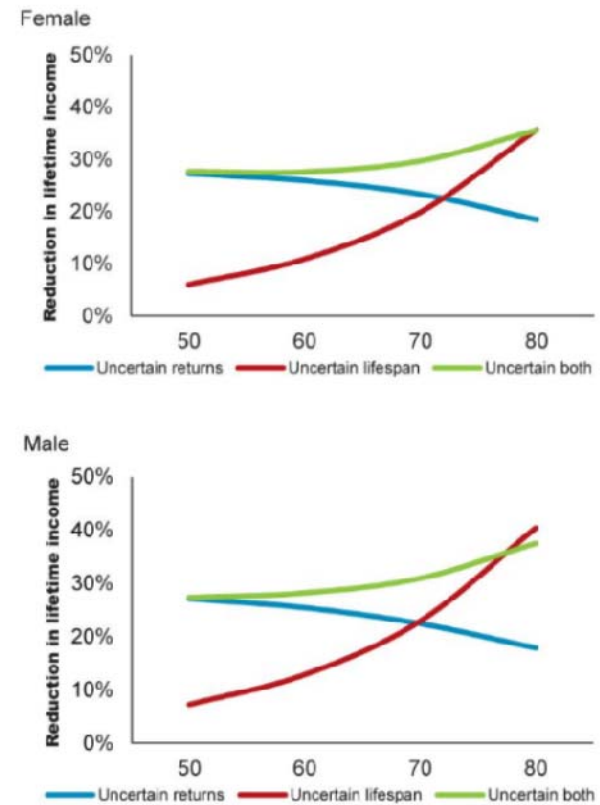
*How Big Is Longevity Risk*

By Bob Collie, FIA

AAll Journal

October 2015

Figure 5. Impact of Uncertainty on Lifetime Income





## Regulatory Guidance on Guaranteed Income Products as Default Options

- IRS Notice 2014-66 outlines circumstances under which TDFs can restrict participation in designated age-bands to invest in annuities
- October 23, 2014 DOL Information Letter to Mark Iwry, Deputy Assistant Secretary for Retirement and Health Policy at the Department of Treasury, describes circumstances when unallocated deferred annuity contracts can be used in a QDIA
- August 2015 GAO report, 401(K) Plans – Clearer Regulations Could Help Plan Sponsors Choose Investments for Participants, cites a need for greater clarity from the DOL regarding use of lifetime income solutions in QDIAs
- December 22, 2016 DOL Information Letter to TIAA provides greater clarity about the use of annuities as default options even when they don't meet the requirements of a QDIA and expresses support for lifetime income options



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## **Guaranteed Income Solutions**

## Interest in Guaranteed Income from DC Plan Sponsors catching-up with Participants

- April 17, 2013 Transamerica survey– According to a survey of defined contribution plan participants by Transamerica Retirement Solutions, 65 percent of participants age 50 or older are interested in having a guaranteed income option in their defined contribution (DC) plan; and 43 percent said if they had the choice, they would invest in one now.
- “Of 212 companies surveyed in 2016, 85% agreed that the “core purpose” of workplace retirement plans should be to serve as a source of retirement income. That’s way up from only 9% in 2012, according to two studies conducted for MetLife.” <sup>1</sup>

<sup>1</sup> EMPLOYERS ARE TRYING TO SOLVE THEIR WORKERS' RETIREMENT INCOME PROBLEM, MARKETWATCH.COM MARCH 2017



## DC Plan Retirement Income Options<sup>1</sup>

- Systematic withdrawals
  - Self-managed
  - Advisory service or managed payout
- Deferred Fixed Income Annuity
- Immediate Fixed Income Annuity
- Immediate Variable Income Annuity
- Immediate Inflation-Adjusted Income Annuity
- Guaranteed Minimum Withdrawal Benefit Annuity

<sup>1</sup> AMERICAN FUND DISTRIBUTORS, INC.

## Characteristics of options

Criteria	Systematic withdrawals						
	Self-managed	Advisory service or managed payout	Deferred fixed income annuity	Immediate fixed income annuity	Immediate variable-income annuity	Immediate inflation-adjusted income annuity	Guaranteed minimum withdrawal benefit annuity
Lifetime guarantee	No	No	Yes	Yes	Yes	Yes	Yes
Pre-retirement protection	No	No	Yes	No	No	No	Yes
Post-retirement increase potential	Yes <sup>1</sup>	Yes <sup>1</sup>	No	No	Yes <sup>1</sup>	Yes <sup>3</sup>	Yes <sup>2</sup>
Post-retirement protection	No <sup>1</sup>	No <sup>1</sup>	Yes	Yes	No <sup>1</sup>	Yes	Yes
Access to savings	Yes	Yes	No	No	No	No	Yes <sup>4</sup>
Inheritance potential	Yes	Yes	No	No	No	No	Yes <sup>4</sup>
Investment control	Yes	No <sup>5</sup>	No	No	Yes <sup>6</sup>	No	Yes <sup>6</sup>
Withdrawal control	Yes	No <sup>5</sup>	No	No	No	No	Yes <sup>7</sup>

<sup>1</sup> Depends on investment performance

<sup>2</sup> Depends on investment performance and contract rules

<sup>3</sup> Depends on measure of inflation used in annuity contract

<sup>4</sup> Subject to contract rules, subject to fees and adjustments in account value

<sup>5</sup> No control while participant transfers control to advisory service; participant can withdraw funds from service at any time

<sup>6</sup> Depends on contract provisions; for guaranteed minimum withdrawal benefit (GMWB) annuities, limits may exist for allocation to stocks. Annuities are subject to the claims-paying ability of the insurer.

<sup>7</sup> Amounts in excess of guaranteed amount may be withdrawn, but adjustments and penalties may apply

Source: "The next evolution in defined contribution retirement plan design," Stanford Center on Longevity and the Society of Actuaries Committee on Post-Retirement Needs and Risks, September 2013.

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## DC Plan Retirement Income Option Tradeoffs

Certainty vs. Liquidity/Flexibility

Optionality vs. Cost



## Concerns with Guaranteed Income Products in 401K Plans

According to Plan Sponsor Council of America's (PSCA)'s [59th Survey of Profit Sharing and 401\(k\) Plans](#), several factors holding back adoption:

- Fiduciary exposure (38.3%)
- High costs (33.3%)
- Operational hurdles such as recordkeeping issues (32.9%)
- Non-portability (28.9%)
- Risk exposure from the insurer guaranteeing the product (26.5%)
- Lack of interest from participants (17.3%)
- “not the role of the employer” to provide (13.3%)

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## **Due Diligence on DC Annuity Solutions**

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## Annuity Safe Harbor Requirements

Under the annuity selection safe harbor, the selection of an annuity provider and contract for benefit distributions from an individual account plan satisfies the requirements of section 404(a)(1)(B) of ERISA if the fiduciary:

1. Engages in an objective, thorough and analytical search for the purpose of identifying and selecting providers from which to purchase annuities;
2. Appropriately considers information sufficient to assess the ability of the annuity provider to make all future payments under the annuity contract ;
3. Appropriately considers the cost (including fees and commissions) of the annuity contract in relation to the benefits and administrative services to be provided under such contract;
4. Appropriately concludes that, at the time of the selection, the annuity provider is financially able to make all future payments under the annuity contract and the cost of the annuity contract is reasonable in relation to the benefits and services to be provided under the contract; and
5. If necessary, consults with an appropriate expert or experts for purposes of meeting these conditions.

Ongoing requirement to review selections.

Focus on the process, not the results, and information available at the time decisions made.



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## Safe Harbor Interpretation

While the Department of Labor (“DOL”) has provided a safe harbor regulation under ERISA for the selection of annuity providers, it does not provide a true roadmap for fiduciaries to follow. (The DOL has indicated that the steps described in the regulation are not the exclusive means of engaging in a prudent selection process.) **It appears, however, that if a fiduciary selects a well regarded company from among the available candidates that others have chosen in the past** – especially one that has a well-known reputation, a significant volume of annuity business and a history of managing that business, high ratings from the ratings agencies that are consistent across all the agencies and over a long period, and is well financed – **it is not necessary to engage in the exact steps described in the regulation.**<sup>1</sup>

<sup>1</sup>LIFETIME INCOME IN DEFINED CONTRIBUTION PLANS: A FIDUCIARY APPROACH A WHITE PAPER BY FRED REISH, BRUCE ASHTON AND JOSEPH FAUCHER



## Due Diligence Approach

Based on plan demographics/participant needs, identify the appropriate income options for the plan.

Once the option type is selected, evaluate using an objective, thorough, analytic process for selection:

### Sample Checklist

- Strength and Stability<sup>1</sup>
- Ratings<sup>1</sup>
- Track Record<sup>1</sup>
- Costs<sup>1</sup>
- Transparency<sup>1</sup>
- State Guarantees<sup>1</sup>
- Recordkeeper availability
- Portability

<sup>1</sup>LIFETIME INCOME IN DEFINED CONTRIBUTION PLANS: A FIDUCIARY APPROACH A WHITE PAPER BY FRED REISH, BRUCE ASHTON AND JOSEPH FAUCHER



## Reference Materials

Internal Revenue Bulletin: 2014-30 on Qualified Annuity Longevity Contracts

[https://www.irs.gov/irb/2014-30\\_IRB/ar07.html](https://www.irs.gov/irb/2014-30_IRB/ar07.html)

Internal Revenue Bulletin: 2014-66 on Lifetime Income Provided Through Target Date Funds in Section 401(k) Plans and Other Qualified Defined Contribution Plans

<https://www.irs.gov/pub/irs-drop/n-14-66.pdf>

Lifetime Income in Defined Contribution Plans: A Fiduciary Approach A WHITE PAPER BY FRED REISH, BRUCE ASHTON AND JOSEPH FAUCHER

<https://www.tiaa.org/public/pdf/LifetimeIncomePaper.pdf>

Qualifying\*Longevity\* Annuity\*Contracts Frequently Asked Questions (FAQs) from DCIIA

[http://www.dciia.org/assets/Publications/2014/white%20paper\\_dciia\\_qualifying%20longevity%20annuity%20contracts%20-%20answers%20to%20frequently%20asked%20questions%20faqs\\_12.2014.pdf](http://www.dciia.org/assets/Publications/2014/white%20paper_dciia_qualifying%20longevity%20annuity%20contracts%20-%20answers%20to%20frequently%20asked%20questions%20faqs_12.2014.pdf)



## Questions

Additional information on fiduciary trends can be found at

fi360 Fiduciary Talk Podcast

[www.fi360.com/fiduciarytalk](http://www.fi360.com/fiduciarytalk)

Also available on iTunes

and

fi360 Blog

[www.fi360.com/blog](http://www.fi360.com/blog)

Additional questions can be directed to [support@fi360.com](mailto:support@fi360.com)