Lifetime Income Solutions as a Qualified Default Investment Alternative (QDIA) – Focus on Decumulation and Rollovers

Presentation by Ted Goldman, Senior Pension Fellow, American Academy of Actuaries to the ERISA Advisory Council, US Department of Labor

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The American Academy of Actuaries is a 19,000-member professional association whose mission is to serve the public and the U.S. actuarial profession. For more than 50 years, the Academy has assisted public policymakers on all levels by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.
Lifetime Income Risk Joint Task Force

- Formed to address the risks and related issues of inadequate guaranteed lifetime income among retirees
- Joint effort of two practice areas:
  - Pension
  - Life
Agenda

- Context
- Academy’s Position Statement on lifetime income in defined contribution (DC plans)
- Perspectives on Qualifying Longevity Annuity Contracts (QLACs)
- Open retiree multiple employer plans (Open Retiree MEPs)
- Additional Academy resources
Context

Car parts

Retirement parts
The Academy’s Position Statement

- The American Academy of actuaries supports policy and educational initiatives that increase the availability of retirement income options within employer-sponsored defined contribution (DC) plans.

- These options, based upon actuarial principles, can help retirees manage their financial security over their remaining lifetime.

The cost of the shift

Past: Defined Benefit (DB) plans a key component of employer-provided retirement benefits
- Paid for and fully managed by employer
- Benefits provided as guaranteed lifetime income
- Pooling longevity risk → efficiency into lifetime income for employees

Current: Shift to DC plans as primary/only source of employer-provided retirement benefit
- Benefits typically paid in the form of a lump sum
- Individuals manage their own lifetime income, investment, and longevity risks
- Loss of efficiency and institutional management → lower retirement income
Key components for income options

- Education throughout the participant’s working career
- Income options that meet retiree needs
- Enabling policies such as safe harbors
The benefits of income options in DC plans

Pricing efficiency
• Longevity risk pooling and institutional pricing

Ease of Transaction
• No need to perform Individual Retirement Arrangement (IRA) rollover to add annuity

Provider and product due diligence
• Minimizes poor choices in provider and product selection

Guidance
• Access to advisors for retirement income planning and longevity risk management options
QLACs

Advantages

• Manages “tail” risk
• Allows more aggressive investment strategies
• Lower premium vs immediate annuity
• Priced to reflect retiree’s circumstances
• Can have greatest value for certain individuals

Deterrents to Usage

• Regulatory/legislative restrictions
• Insurance companies see low demand; minimal marketing and consumer education
• Advisers -- generally low utilization of annuities
• Individuals see possible loss of premium
• Plan sponsors concerns (administrative complexities, low demand, portability, fiduciary risks)
How to increase attractiveness of QLACs

- Add flexibility
  - Allow variable/index-based returns
  - Eliminate unisex pricing;
  - Allow aggregation for 25% rule
- Modify annuity selection safe harbors
- Consumer education
  - Starting with efforts by the Department of Labor (DOL)
How much a $100,000 QLAC provides

Note: Amounts represent market rates for IRAs from publicly available sources on-line. If paid from a 401(k) plan a unisex basis would have applied (resulting in amounts between those shown).

<table>
<thead>
<tr>
<th>Annual Income</th>
<th>Female Age Payment Begins</th>
<th>Male Age Payment Begins</th>
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</thead>
<tbody>
<tr>
<td>$0</td>
<td>65</td>
<td>65</td>
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<tr>
<td>$5,800</td>
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<td>$6,200</td>
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$20,600 $33,600 $6,500 $23,900 $42,200

$5,000 $17,000 $26,900 $18,700 $31,500

$20,600 $33,600 $6,500 $23,900 $42,200

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Open Retiree Multiple Employer Plan

Open Retiree MEP
- Administration
- Communication
- Education
- Decumulation strategy
- Vetting and selection
- Decision-making (i.e. Social Security & Medicare)

Retirement Marketplace
- Asset management
- Annuities

Employer A
Employer B
Employer C
Employer D
Retiree Accounts
## Advantages of Open Retiree MEPs

<table>
<thead>
<tr>
<th>Retirees</th>
<th>Plan Sponsors</th>
</tr>
</thead>
<tbody>
<tr>
<td>□ Large plan offerings and pricing</td>
<td>□ Minimize fiduciary risk</td>
</tr>
<tr>
<td>□ Spur development of drawdown and risk pooling strategies</td>
<td>□ Offer best-in-class services to retirees</td>
</tr>
<tr>
<td>□ Critical conflict-free decision-making support</td>
<td>□ Focus on core mission</td>
</tr>
</tbody>
</table>
Summary

- Converting lump sums to lifetime income will continue to be an issue even upon the adoption of lifetime income QDIAs
- QLACs can be a valuable alternative for select retirees
- Open Retiree MEPs could improve decumulation decision-making
Questions?

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