Providing incentives for annuities within retirement plans

To mature into a strong safety net, workplace retirement plans must be able to deliver guaranteed lifetime income

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TIAA was founded 100 years ago by Andrew Carnegie to provide college professors with retirement income through employment-based annuities. This was an innovative concept for the time, predating the Social Security system by two decades.

The first product was a low-cost in-plan annuity option offering safety, stability and guaranteed income for life. The annuities sold by TIAA became the model for the tax-deferred annuities that form the basis of Section 403(b) of the tax code.

Today, the retirement industry is focused on how to translate retirement savings into income that will last for life.

There are several reasons for this — in our country, 10,000 people turn 65 each day, and they are living much longer, increasing the amount of time spent in retirement.

There's also been a shift from defined benefit to defined contribution plans that, for most Americans, do not include lifetime income features. This makes the plan design features that Andrew Carnegie built into our plans a century ago all the more relevant. For decades, the higher education sector and others in the nonprofit world have offered plans that provide guaranteed income in retirement that continues to grow when employees change jobs.

For that reason, we believe the not-for-profit sector has insights on how to improve income security in retirement with the broader industry. Annuity products are largely missing from retirement plan investment menus of U.S. corporations, but we feel momentum is building, and we are working to change the dialogue in the industry.

Over the past several years, we have seen 401(k) design and 403(b) design move closer together, and the fact that an entire industry is looking at guaranteed income is a positive sign.

Giving plan participants direct access to annuitization vehicles can reduce the risk of leakage through lump sum distributions — in effect, helping to keep funds meant for retirement available to people when they are ready to retire. And, perhaps most importantly, there is a behavioral psychology opportunity, as in our experience, those who save for retirement using in-plan annuities are more likely to annuitize upon retirement.

Are there some simple changes that could be made to make it easier for Americans to invest in and receive guaranteed income? Consider the current qualified default investment alternative regulation.

Of the potential investment options that qualify under the QDIA safe harbor, the most utilized has been and continues to be target-date funds. In fact, over 75% of defined-contribution plan sponsors electing to use the QDIA safe harbor default their participants into target-date funds, according to a Profit-Sharing Council of America study.

This has helped ensure retirement plan participants are defaulted into diversified and well-managed portfolios, but the overwhelming majority of these default products lack guaranteed annuities within the investment.

In considering this, we found a way to substitute standard bond funds with a guaranteed fixed annuity, providing the option of certainty of income within the familiar target-date structure. This one simple change can better mitigate the real risks people face in retirement planning — including market risk, inflation risk, interest-rate risk and longevity risk — and help deliver the income guarantees many investors think are already in a target-date fund.

Plan sponsors and their consultants can use their own in-house expertise to manage the glide path and investment options to fit the specific demographics of their participants. This is one example of the kind of innovation we believe is needed.

As federal regulators increasingly appreciate the need for in-plan lifetime income, they are reconsidering ways to include annuities and similar options in retirement plans.

The **Department of Labor** identified "the need for lifetime income as an important public policy issue" and emphasized its support for initiatives "that could lead to broader use of lifetime income options in defined contribution plans as a supplement to and enhancement of accumulation of retirement savings." There is a growing interest in bipartisan solutions to address these issues.

To mature into the strong safety net that an aging society requires, workplace retirement plans must be able to deliver guaranteed lifetime income. This means giving financial instruments that are uniquely qualified to guarantee income in retirement a prominent role in plans. What can and should be done is to remove impediments to annuity adoption by employers and provide incentives for annuity selection by employees.

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