

WHITE PAPER

Navigating the market for guaranteed lifetime income products

A guide on how to evaluate and determine the most suitable in-plan annuity option, or options, available for a plan

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Comparing apples to oranges

HOW RETIREMENT INCOME SOLUTIONS DIFFER FROM TRADITIONAL DEFINED CONTRIBUTION PLAN INVESTMENTS

Retirement is a time of great opportunity and independence that many plan participants look forward to. It's a moment of relaxation, quality time with friends and family, and freedom to pursue new and lifelong passions. However, it's also a milestone that requires significant financial planning and thought. How much a participant has saved and how those investments have performed over time can significantly affect participants' ability to enjoy the retirement they have envisioned.

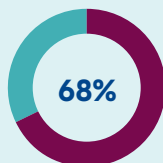
Incorporating a guaranteed lifetime income solution, such as an annuity, into a plan can help participants build and protect income that supports their retirement goals. These solutions are intended not to replace, but rather to augment traditional defined contribution (DC) plan investments for a holistic strategy that balances both growth and protection, helping participants plan for their unique priorities.

Traditional DC Plan Investments	Guaranteed Lifetime Income Solutions
 • Growth oriented • Directly invested in the market and exposed to market risk • Accumulation focus • Early/middle of career	 • Income oriented • Most are not directly invested in the market and therefore limit exposure to market risk • Decumulation focus • Late in career/retirement

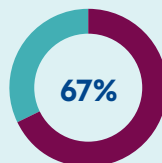
Just like apples and oranges are both part of a healthy diet, traditional DC plan investments and retirement income solutions are key elements of a sound retirement strategy, which support a participant's goals in both the accumulation and decumulation phase.

More plan participants interested in guaranteed lifetime income solutions

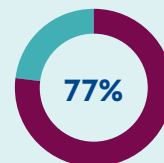
As the outlook on retirement shifts, more individuals are recognizing the value of having a reliable income stream that lasts throughout their lifetime, as evidenced by a growing interest in in-plan annuities.



68% would like **more information about annuities** as part of their plan.¹



67% would consider **adding an annuity to their plan** if it was available.¹



77% say an option to **build a protected foundation for lifetime income** would increase their loyalty to their employer.¹

¹ Allianz Life conducted an online survey, the 2023 2Q Quarterly Market Perceptions Study, in May 2023 with a nationally representative sample of 637 respondents age 18+ with an employer-sponsored retirement plan.

Comparing apples to apples

FRAMEWORK FOR EVALUATING RETIREMENT INCOME SOLUTIONS

There are over 7,500 varieties of apples in the world. While there aren't nearly as many retirement income solutions, it's a growing field and the intricacies of product features can make it difficult to navigate. To help you find the best fit for your clients' appetites, this white paper weighs the benefits and drawbacks of different retirement income solutions.

Weighing the benefits and drawbacks

For this white paper, six characteristics were identified that align with key pain points that retirees and pre-retirees face throughout their lifetimes. These will act as our guardrails for evaluating the overall effectiveness of different guaranteed lifetime income solutions.



Protection from market downturns: The majority of Americans are cautious about investing and want solutions that help protect a portion of their savings from market loss. 66% of Americans are keeping more money out of the market than they think they should because they're worried about loss.¹



Increasing income potential: Nearly eight in 10 Americans are concerned that the rising cost of living will affect their retirement plans. Products that provide the potential for increases may provide some level of security against the corrosive impacts of inflation.¹



Flexibility: With more workers following less linear career pathways with more frequent on and off ramps throughout their career, it's important that they have flexibility in how they contribute to and take income.



Accessibility: We know that emergencies happen. Limited access to cash can be a drawback for plan participants when considering a guaranteed lifetime income solution. Nearly half (47%) of plan participants identified the ability to access their money without penalty as one of the three criteria for selecting a guaranteed lifetime income option.²



Portability: It's important that guaranteed products stay true to their promises regardless of changing circumstances. If a participant leaves the plan, or the plan makes a change, guaranteed products should be portable.



Cost: Fees are a consideration for any plan investment, including guaranteed lifetime income products. When evaluating cost, it's also important to consider the value a participant receives from the product. In fact, half of plan participants agree that higher fees are worth it for a guaranteed lifetime income option.²

¹Allianz Life conducted an online survey, the 2023 2Q Quarterly Market Perceptions Study, in May 2023 with a nationally representative sample of 637 respondents age 18+ with an employer-sponsored retirement plan.

²2022 In-Plan Insights Survey of Plan Participants, Greenwald Research, November 2022.



No one size fits all

While the identified characteristics provide a framework, it is essential to approach retirement planning with inclusivity and acknowledge the unique nature of each individual's retirement journey. In recognizing that what works for one person may not be ideal for another, it's possible to identify solutions that align with unique financial goals, aspirations, and risk tolerances.

The intent is to unpack the range of options available and provide guidance on how to determine the most suitable option or options available for a plan, first by exploring the different annuity types and then by detailing the various ways to implement an annuity in a DC plan.

ANNUITIZATION VS. GUARANTEED LIFETIME WITHDRAWALS

Before shifting attention to the various types of annuity products, it's important to make a distinction between pure annuitization products and those that come with a Guaranteed Lifetime Withdrawal Benefit (GLWB). This differentiation plays a significant role in addressing one of the most common criticisms of annuities, which is their perceived rigidity and irrevocability.

Annuitization

When someone thinks of an annuity, oftentimes pure annuitization products are what come to mind. Annuitization is the process by which the value of the annuity is converted into a stream of income that is paid out over a fixed period, or for life. Payments are determined based on premiums paid, life expectancy, and the annuity's growth rate. The certainty and security of annuitization can help participants fund basic living expenses in retirement. However, the decision to annuitize is typically an irrevocable decision that cannot be reversed or changed in any way. This means that the participant cannot access the cash value of their annuity. If an unexpected expense comes up, they cannot make a withdrawal from their annuity.

Guaranteed Lifetime Withdrawal Benefit

In comparison, a Guaranteed Lifetime Withdrawal Benefit (GLWB) is a rider, either built in or available at an additional cost, which enables the annuity owner to begin receiving payments without having to give up access to the remaining cash value of their account. This means, should a participant need to make a full or partial withdrawal of their account, they have the opportunity to do so, often with no surrender charge. Taxes and Market Value Adjustment (MVA) may apply to either a full or partial withdrawal.

With the rising costs of health care and long-term care, and unanticipated life events that can significantly alter a participant's financial situation – such as the death of a family member or a divorce – this feature provides a safeguard for those who need it. The GLWB design not only allows those who need to take cash out of their contract to do so, but it also provides the flexibility to delay or even pause income payments, which can be taken later on. As lifespans increase and career pathways become less linear, some participants may still be actively working and may not require income right away. In this case, delaying or pausing payments could result in more income later on when it's needed, or a larger bequest for loved ones.

With a GLWB, participants have the option to receive lifetime withdrawal payments, which may include opportunities to increase income – offering participants the chance to earn more income in future years to help counter inflation. Overall, the GLWB design ushers in a new level of innovation and flexibility that can help address a number of historical barriers and pain points associated with annuities.

A COMPARISON OF UNDERLYING ANNUITY PRODUCTS

The following section examines various annuity types and their respective advantages and disadvantages. For the purposes of this white paper, the focus is broadly on fixed annuities, variable annuities, and fixed index annuities. Within each of these broad categories, there are a range of products, some of which are identified in the section to the right.

Fixed annuities

A fixed annuity is a financial product that provides stable, guaranteed retirement income either for a set period or for the rest of a plan participant's life. The value of a fixed annuity increases over time based on a fixed rate, and is converted into income through a process known as "annuitization." This provides a level of predictability, but may also be rigid and inflexible.

Variable annuities

Variable annuities, or VAs, are typically asset accumulation products, and are the predominant form of annuities found in DC plans. Instead of being used for the purchase of income rights as under a fixed annuity, they are designed to give participants the option to direct their account balances to various investments. These investments typically include "pooled separate accounts" and an insurance company's fixed account.

One of the key features of pooled separate accounts in VAs is that they offer the potential for a higher level of income compared to traditional fixed annuities. This is because of the performance of the separate accounts. However, VAs also come with increased risk, as returns are determined by how well these investments perform.

Fixed index annuities

Fixed index annuities, or FIAs, provide a unique advantage by shielding participants from direct exposure to stock, equity, or bond investments, effectively eliminating market risk. Instead, they offer the opportunity to earn interest based on positive movement in a market index, like the S&P 500®, up to a limiter. FIAs serve as a middle ground between traditional fixed annuities and variable annuities, offering interest potential while still providing protection from market downturns.

Most common annuities in the DC market

Within the DC space, products may be in-plan or plan-adjacent. The focus of this white paper is on in-plan products, wherein participants contribute gradually over time by directing a percentage of their DC plan contributions to an annuity.

Other solutions may be plan-adjacent, where participants use funds from their qualified plan to purchase an annuity upon reaching retirement age – often as a lump sum. These plan-adjacent solutions are typically fixed annuities that require annuitization.

FIXED

- Deferred Fixed Annuity
- Deferred Income Annuity (DIA) including Qualified Longevity Annuity Contracts (QLAC)

VARIABLE

- Variable Annuities with GLWB

FIXED INDEX

- Fixed Index Annuities with GLWB
- Fixed Index Annuities with annuitization

HOW DO FIXED ANNUITIES STACK UP?

The descriptions provided here are representative of a range of fixed annuity products available in the market today and are not meant to refer to any specific product. The key below is an assessment of how well these products address the pain points identified in the framework of this paper.

● **Protection from market downturns**

Fixed annuities can be an attractive option for participants who want to convert savings into a predictable stream of income without having to worry about market fluctuations. They are not invested in the market and are fully protected from market risk. Instead, fixed annuities grow based on a fixed interest rate.

● **Increasing income potential**

The fixed annuity's income payout remains the same throughout a participant's life, which may prove insufficient in an elevated inflationary environment. Some may offer a cost-of-living-adjustment (COLA) option that grows at a specified rate, but then offers a lower starting payment to offset increasing income.

● **Flexibility**

Because payouts from fixed annuities require annuitization, the participant cannot access the lump sum or make changes to the annuity's terms after payments have begun. With a deferred income annuity, including QLACs, there is additional rigidity because the start date for income is predetermined at the time of purchase, so participants cannot withdraw money early or borrow against their premiums. As a result, there is an added risk that the participant could pass before their income begins. SPIAs are also relatively inflexible when it comes to starting income, typically stipulating that the annuitant begin receiving income immediately, or within one year of purchase.

● **Accessibility**

Since these products are annuitized, the annuitant cannot access the cash value of their annuity in the event of emergencies. Changing life circumstances can come with unexpected expenses, and many participants place a premium on having an avenue to access cash should they need it.

● **Portability**

If a fixed annuity is set up as an individual contract, or can be converted to an individual annuity from a group contract, it may be portable to an IRA. However, they are generally not portable to other retirement plans, and costs, benefits, and guarantees may change when moved out of plan. Those embedded in Collective Investment Trusts (CITs) may face additional portability constraints due to their contractual complexity and other structural limitations. Out-of-plan or plan-adjacent products are inherently portable, but because they are typically purchased at or near retirement age, it is unlikely participants will be able to carry this benefit with them throughout their careers.

● **Cost**

Fixed annuities generally don't come with an explicit cost and can therefore be a cost-effective option. However, cost can also be assessed by determining how much income an annuity can generate from the premiums paid into it. By projecting income over life expectancy or to a typical planning age, the cost or relative efficiency of one annuity can be compared with another.

HOW DO VARIABLE ANNUITIES STACK UP?

The descriptions provided here are representative of a range of variable annuity products available in the market today and are not meant to refer to any specific product. The key below is an assessment of how well these products address the pain points identified in the framework of this paper.

- **Protection from market downturns**

The investments made into a VA are held in separate accounts and are not typically protected from market loss. While many in-plan VAs protect against losses on the value used to determine what the retirement income payments will be, any market declines and fees typically have to be recouped before additional gains can be added to this value. Further, full or partial withdrawals prior to income beginning typically have no principal protection.

- **Increasing income potential**

Since variable annuities are linked to market performance, positive returns on investments can increase income. However, past losses, fees, and lifetime payouts would need to be surpassed by positive returns in order for income to increase.

- **Flexibility**

Most in-plan variable annuities on the market include a GLWB benefit that is either built in or available at an additional cost. The GLWB design provides enhanced flexibility, so participants can choose how and when to take income depending on their own unique circumstances and plan specifications.

- **Accessibility**

With variable annuities that include a GLWB, the participant retains access to the cash value of their annuity. This means the participant can take a full or partial withdrawal, often without a surrender charge. Note that in-plan VAs typically do not protect the principal or account value from market loss. Therefore, a full or partial withdrawal may result in a value less than what was originally invested or a previous higher market value. Taxes may also apply.

- **Portability**

While the value of the account balance within a VA's separate account is freely portable to IRAs or other plans, the accumulated income benefits may be subject to plan and product limitations. For example, many of the variable annuities on the market today are offered as group annuities. When rolled out of plan, the cost, benefits, and guarantees are subject to change. Further, the application of securities laws may also prevent rolling any accumulated guarantees associated with a VA into an IRA or certain kinds of retirement plans.

- **Cost**

There are typically a variety of fees in a VA, including GLWB income rider fees, mortality and expense risk charges, contract charges, administrative processing expenses, and separate account investment management fees. Explicit fees are typically much higher for VAs than other in-plan annuity types. However, as noted previously, overall costs can also be assessed by determining how much income the annuity is likely to generate over time.

HOW DO FIXED INDEX ANNUITIES STACK UP?

The descriptions given here are representative of a range of fixed index annuity products available in the market today and are not meant to refer to any specific product except where noted. Assessments based on the key below are specific to the Allianz Lifetime Income+® Annuity, and are not necessarily representative of the whole range of FIAs available in the market.

● **Protection from market downturns**

Account balances in an FIA are not directly invested in stocks or bonds, or in a “pooled separate account.” Instead, the annuity can earn interest based on changes in a market index (e.g., the S&P 500®).

When index performance is positive, the participant receives indexed interest based on a participation rate, or a cap or other limiter. This interest is locked in and cannot be lost in the future due to any index decline. If the index performance is negative, nothing happens, and the annuity’s value can never decline due to a market downturn. Note that product or rider fees may reduce contract values. This means that plan participants never have to make up index losses before they can start earning positive interest.

● **Increasing income potential**

In addition to the potential to earn positive interest, some FIAs with GLWBs offer additional opportunities for income growth. Some offer this only during the accumulation phase, whereas others, such as the Allianz Lifetime Income+® Annuity with Lifetime Income Benefit, provide opportunities for increasing income on the payments they receive throughout retirement – even if the participant’s annuity balance drops to \$0.

● **Flexibility**

Similar to VAs, most in-plan FIAs include a GLWB benefit that is either built in or available at an additional cost, providing enhanced flexibility so participants can choose how and when to take income depending on their own unique circumstance and plan specifications. The Allianz Lifetime Income+® Annuity offers a built-in GLWB at no additional cost with the flexibility to choose when to start income (after age 60) and stop or pause payments, which can be taken later on.

● **Accessibility**

FIAs with a GLWB allow participants to access the cash value of their annuity. This means that the participant can take a full or partial withdrawal, typically without a surrender charge. Taxes and Market Value Adjustment (MVA) may apply.

● **Portability**

Portability may be subject to plan and product limitations. While some of the FIAs on the market today are offered as group annuities, the Allianz Lifetime Income+® fixed index annuity is set up as an individual contract, which means it can offer plan and participant-level portability. All benefits, pricing, and guarantees carry with the contract and will not change regardless of changing circumstances.

● **Cost**

FIAs with GLWBs are typically lower cost than VAs with GLWBs. The explicit cost of an FIA with GLWB may be higher than a fixed annuity depending on riders. However, it’s worth noting that an FIA with a GLWB typically includes built-in features that would come at an additional cost on a traditional fixed annuity, such as COLAs or other riders. As noted, the cost of a particular FIA can be compared to other FIAs or annuity types by determining how much total income it is likely to generate over a given timeframe.

Implementing guaranteed lifetime income solutions

Every apple begins as a seed. Just as the right combination of environmental factors nurtures these seeds into apple trees, the method by which a product is delivered in a retirement portfolio can significantly impact its effectiveness in serving an individual's needs.

For this reason, it is important to carefully consider the unique features of each method of delivery when deciding which option is appropriate for a plan. In the following section, we will examine the benefits and drawbacks of each option to provide a comprehensive understanding of how each implementation option can complement the goals of your plan sponsor clients and their participants.



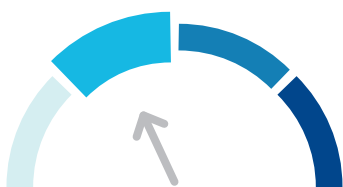
Level of personalized advice: Low

UI may include some calculators or tools to provide guidance, but ultimately all investment decisions are made by the participant.

Annuity as a standalone investment option

Offering an in-plan annuity as a standalone investment option means the annuity is added to a retirement plan's fund lineup, allowing the participant to decide what percentage of their assets they want to allocate. This option works best for investors who prefer to make and monitor their own investments.

Recent strides in technology and user experience have streamlined the incorporation of annuities into recordkeepers' interfaces and made it easier for participants to make informed decisions. This may include calculators and various visual cues to let participants know if they're on track. Other tools exist to support how plan sponsors want to make these available, such as built-in contribution limits.



Level of personalized advice: Moderately low

Allocations are based on participant's retirement age.

Target Date Fund

Target Date Funds are a popular choice for investors who are comfortable with limited personalization and want to "set and forget" their retirement portfolios. The primary goal of a TDF is to provide a diversified investment portfolio that gradually rebalances and reallocates the fund's assets over time, becoming more conservative in the years leading up to retirement to hedge against market risk. However, market risk is not the only risk that retirees face.

Embedding an annuity within the TDF series enables participants to hedge against another risk: longevity. This strategy involves gradually allocating funds to an annuity during the years leading up to retirement, thereby safeguarding a portion of assets that will be dispersed as a reliable income stream during retirement. However, the traditional target date model limits the flexibility to customize the terms of the annuity to align with unique retirement income needs, as it is solely based on age.



Level of personalized advice:
Moderately high

Uses data points from the recordkeeper and plan sponsor to build a personalized glide path.

Personalized TDF

As lifespans increase, longevity risk is becoming a primary concern for participants, but it is not the only risk in play. Unlike traditional TDFs that hinge solely on an individual's age, a personalized TDF considers a broader range of data points to tailor the asset allocation so that it suits the participant's unique risk-and-return needs. It's easy to implement, like a traditional TDF, but also incorporates additional parameters such as salary, retirement balance, contribution rate, and employer match percentage.

Annuities are intended to provide income for life, but they also help address a number of risks that participants face throughout their lifetime. An in-plan annuity through a personalized TDF could be an effective solution for delivering guaranteed lifetime income with allocations based on a more targeted risk profile. This is still an emerging space, but well-positioned for growth given the popularity of Target Date Funds and an increased demand for products that offer both personalization and protection.



Level of personalized advice:
High

May offer more personalized inputs plus opportunities for plan participants to engage for even more personalization.

Managed Account

A Managed Account is a personalized advice program offered within a 401(k) plan that makes investment decisions on behalf of a plan participant. They are based on computerized algorithms that work in tandem with the expertise of investment professionals who actively manage the portfolio. These programs typically offer the highest degree of personalization by offering guidance that adapts to match each participant's unique financial situation and retirement goals.

Delivering a guaranteed lifetime income program through a managed account provides participants with a way to build a protected foundation for retirement income that's designed for their needs. Unlike other implementation options, a managed account is an approach based on individuals, not averages. Participants even have opportunities to engage by contributing supplementary information about outside assets, priorities, and retirement goals through an optional survey.

Since they are professionally managed and regularly monitored, managed account programs can respond to changes in a participant's financial situation or priorities. Paired with a guaranteed lifetime income solution featuring a GLWB – which allows participants or the managed account acting as their fiduciary to decide when and how to contribute and take income – this combination may provide an unparalleled level of flexible, personalized advice.

Have you considered ...?

Additional points to consider when designing a guaranteed lifetime income program

How a guaranteed lifetime income program works in the context of a Collective Investment Trust (CIT)

Collective Investment Trusts (CITs) are becoming increasingly popular in DC plans, as they come with lower costs and more flexibility than mutual funds. For this reason, many guaranteed lifetime income solutions developed in the wake of the SECURE Act of 2019 have been designed for use with CITs. However, when considering a guaranteed lifetime income solution in the context of a CIT, there are several factors that plan fiduciaries should consider. Notably, an arrangement where a CIT purchases the insurance guarantees to provide a GLI program may limit portability and the personalization of guarantees. The complex nature of such arrangements may also produce challenges when it comes to the management and fiduciary oversight of the CIT-embedded GLI programs. It is important to be aware of these concerns. An alternative option to consider is the direct purchase of a GLI by the plan, which can be managed alongside the CIT, but addresses many of the barriers of the former approach.

→ **LEARN MORE** about considerations for CIT/GLI programs in the white paper **“Assessing Guaranteed Lifetime Income Programs Utilizing CITs”** from Robert Toth, Principal at the Law Office of Robert J. Toth, Jr., LLC.

In-plan vs. out-of-plan

A vast majority of plan participants (78%) prefer to make gradual contributions over time rather than a one-time lump sum payment.¹ This preference is stronger among participants with less than \$1M in investable assets (80%) compared to those with over \$1M in assets (60%).¹ This underscores the value of the in-plan approach where individuals contribute a percentage of their retirement plan allocations to the annuity each pay period instead of handing over a lump sum of assets at retirement.

Moreover, an in-plan approach can help counteract some of the negative behavioral biases that prevent participants from taking proactive steps to adequately prepare for retirement, even when they know it may be in their best interest. Combining an annuity with a target date fund, personalized target date fund, or managed account could encourage the participant engagement needed to make allocations to the annuity.

The number of GLI options that should be available in a plan

Now that you have a framework for evaluating different lifetime income options, it's important to note that most participants who are interested in guaranteed lifetime income believe their plan should offer more than one option. Three-fourths of participants say there should be two or more options available to them in a plan.¹ This principle could also extend to the ways in which the product is implemented, with some investors favoring a “DIY” approach and others seeking the personalization that comes with a managed account, or personalized TDF. Carefully consider all options and listen to the needs of both plan sponsors and their participants when making a recommendation to a plan.

¹ 2022 In-Plan Insights Survey of Plan Participants, Greenwald Research, November 2022.



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