

**MetLife**

**RETIREMENT INCOME PRACTICES STUDY<sup>SM</sup>**

**12**

Perspectives of Plan  
Sponsors and Recordkeepers  
for Qualified Plans

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<sup>3</sup> As of December 31, 2011.

<sup>4</sup> LIMRA, Group Annuity Risk Transfer Survey, Fourth Quarter 2011.

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# INTRODUCTION

MetLife commissioned this research of the largest U.S. plan sponsors and their recordkeepers to assess whether and to what extent these two groups are communicating about – and closely coordinating their efforts to offer – retirement income education, strategies and solutions for the participants in the defined contribution (DC) plans (including 401(k) plans) that they sponsor and service, respectively. To the best of our knowledge, this is the first retirement income-focused study that examines the dynamics of the plan sponsor-recordkeeper relationship with regard to the provision of lifetime income options.

Specific topics covered in the study include:

- the approaches taken to offer education and tools to enable participants to model their future retirement income needs;
- the correlation between the retirement strategies to which plan sponsors and their recordkeepers gravitate and the types of retirement income solutions being offered to plan participants;
- the most compelling retirement income product features and the top criteria for product evaluation;
- awareness about – and commitment to – industry standards for in-plan solutions; and,
- perceived obstacles to more widespread offering and adoption of products that provide guaranteed lifetime income.

## A CHANGING DEFINED CONTRIBUTION PARADIGM

Several decades after the advent of 401(k) plans and after the burden of retirement started shifting from employer to employee, an increasing number of DC plan participants are beginning to understand that – without a retirement income component – their DC plans are incomplete retirement plans. For instance, MetLife's latest Employee Benefits Trends Study<sup>5</sup> found that among employees who worked for companies with 10,000 or more workers: 54% were worried about having enough steady income in retirement to meet essential expenses such as housing, food

and transportation; 52% were concerned about outliving their retirement money; 46% were worried about needing to continue to work through retirement years; and, 74% expect to receive significantly lower Social Security payments when they retire compared to today's recipients, whether in absolute or relative purchasing power terms. Among those currently age 65, only 45% have fully retired,<sup>6</sup> according to another MetLife study. Additionally, a recent survey from the Employee Benefit Research Institute (EBRI)<sup>7</sup> found that only 14% of current workers are very confident about having enough money for a comfortable retirement, and 46% reported that they were either very or somewhat likely to select a product or option that would provide them guaranteed income for life.

DC plans were originally introduced as supplemental savings programs – often by companies who already provided a defined benefit (DB) plan. They were not intended to serve as an employee's primary source of retirement savings, nor were they designed to provide guaranteed lifetime income. That was the purpose of DB plans. However, as countless studies have pointed out, DB plans, which provide benefits in the form of guaranteed lifetime income, have been on the decline for a variety of reasons. For those DB plans that do remain, many provide lump sum distributions in some form, either by adding a lump sum option to the plan's payout choices or by converting the plan to a "hybrid," lump sum-oriented format. These trends, coupled with continued uncertainty about the future viability of Social Security, are putting increasing pressure on DC plans not only to allow participants to save for retirement but also turn their savings into a monthly income they cannot outlive.

If there is any lesson to be learned from the recent market crisis, it is that managing a retirement portfolio to last a lifetime is difficult for even the most sophisticated investors. Today, not only are a significant number of retirement-eligible workers delaying retirement to recoup their DC plan losses, they also appear to be working longer to save more – fearful that what they have saved may not be quite enough for the 20-30 years or more that they may spend in retirement.

For plan sponsors, many of whom expected DC plans to enable them to provide a savings plan with lower expenses and administrative burdens than those of DB plans, the evolution of the DC plan from a supplemental savings plan to the primary – or, in many cases, the only – retirement plan is changing the nature of their role. This development has coincided with broad-based awareness that the employee choice model under which DC plans were introduced has not, in general, worked particularly well with regard to producing adequate savings for retirement among those who have chosen to participate in them. With this paradigm shift, many plan sponsors are

<sup>6</sup> MetLife Mature Market Institute, *Transitioning into Retirement: The MetLife Study of Boomers at 65*, April 2012.

<sup>7</sup> Employee Benefit Research Institute and Mathew Greenwald & Associates, Inc., *2012 Retirement Confidence Survey*, March 2012.

beginning to recognize that they may have some obligation to ensure that their plans provide the means for their workers to achieve retirement security. Adopting a culture of retirement income, identifying which solutions will be best able to help DC plan participants achieve their retirement income goals, and then using their institutional purchasing power to offer affordable options are all actions within the reach of plan sponsors who want to know that they are maximizing their DC plans to help enable their employees to have access to a secure retirement.

#### APPROACHING A RETIREMENT INCOME CROSSROADS

With widespread industry and increasing government attention paid to retirement income, it is becoming abundantly clear that participants need to start thinking about their need for retirement income – not only at the point of retirement when market conditions and other factors might make such a major decision difficult, but also during their working years. In order to do so, both employers and DC plan recordkeepers have key roles to play to pave the way for participants to take action.

Fortunately for plan participants, the U.S. Treasury Department issued in February 2012 an initial package of proposed regulations and rulings intended to clear the way for millions of Americans to have “better and more accessible retirement income options.”<sup>8</sup> This guidance should have the dual effect of both calling sponsor and participant attention to the importance of lifetime income and encouraging workers to consider securing at least a portion of their retirement savings. The Treasury Department’s actions are also expected to encourage the plan sponsor community and their recordkeepers to take the actions necessary for millions of workers to generate retirement income to last a lifetime.

While retirement plan providers and sponsors are still at the very early stages of enabling DC plans to provide guaranteed lifetime income, we may be approaching a retirement income crossroads. Though obstacles do still exist for more widespread offering of retirement income products – including platform limitations, fiduciary concerns and perceived low demand – none seem insurmountable if there is a strong desire on the part of plan sponsors, their recordkeepers, the consulting community and public policymakers to engage in providing retirement income solutions to plan participants. If these groups work together, then plan participants are the ones who stand to gain the most by knowing that they will be able to maximize what they were able to save during their working years by converting some of that savings as needed to generate a “retirement paycheck.”

<sup>8</sup> U.S. Department of the Treasury, *Treasury Fact Sheet: Helping American Families Achieve Retirement Security*  
By Expanding Lifetime Income Choices, February 2, 2012.

# Key Findings

## PLAN SPONSORS TAKE A SELF-SERVICE APPROACH TO PROJECTING RETIREMENT INCOME BUT RELATIVELY FEW PARTICIPANTS INTERACT WITH THE TOOLS PROVIDED

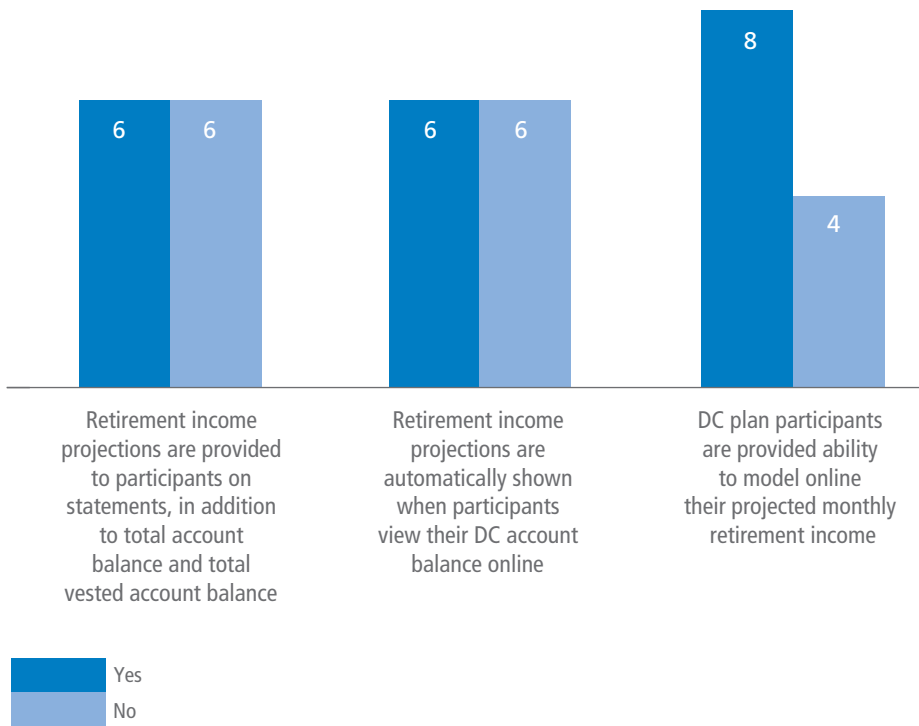
It is often very difficult for plan participants to conceptualize what their DC plan balance can mean in terms of a stream of income for life. While many tools have been developed that will project the amount of monthly income a participant might receive during retirement, our research found that such projections are not automatically shown to participants when they view their account balances online, nor are they routinely provided to plan participants on statements summarizing their total and vested account balances. In fact, only 28% of plan sponsors and six of the 12 recordkeepers say retirement income projections are automatically shown to participants when they view their account balance online.

Similarly, only one-third of plan sponsors (33%) and the same six recordkeepers report that they include retirement income projections on participant statements. When asked why they do not provide income projections to participants (either online or on participant statements), several recordkeepers cited a lack of interest on the part of plan sponsors for showing this to participants. That said, in 2012, four recordkeepers are planning to automatically show projections to participants when they view their account balance online, and two recordkeepers are planning to add retirement income projections to participant statements.



## Retirement Income Projection Options Available to DC Plan Participants

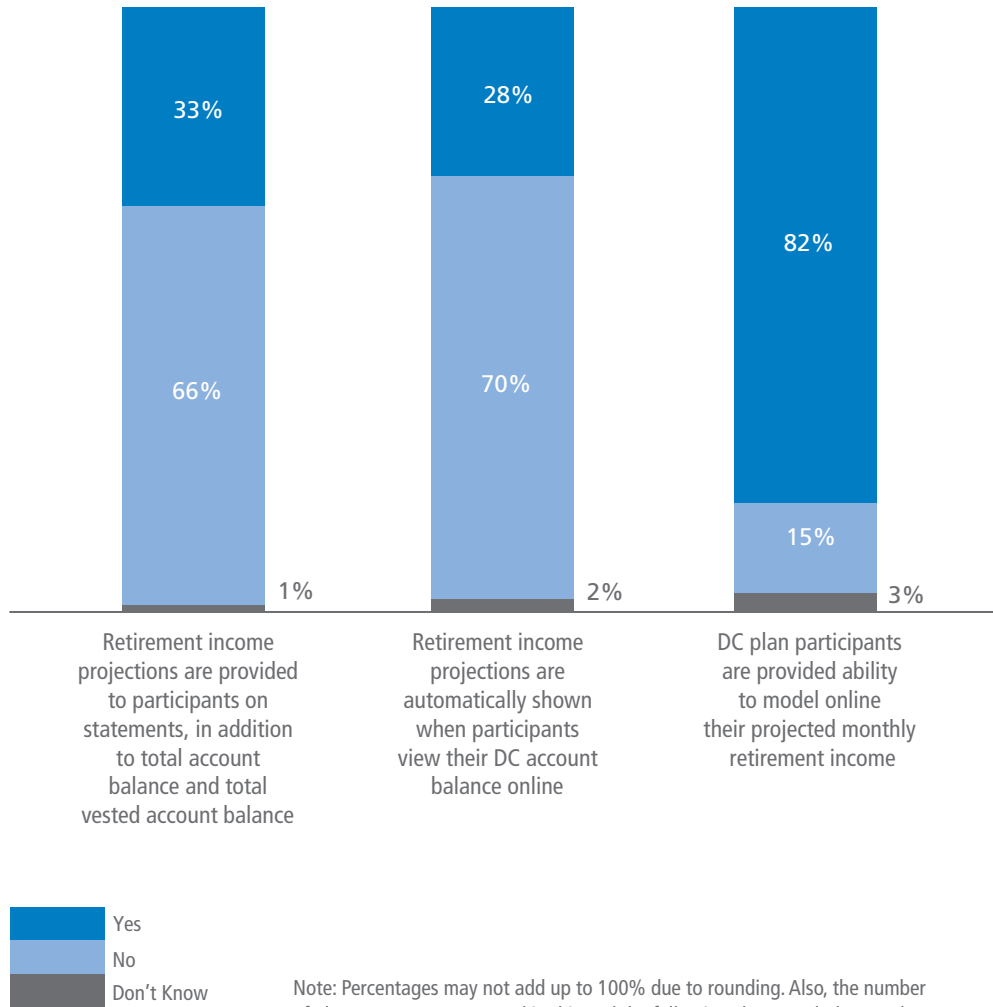
Options Made Available by Recordkeepers (n=12)



Note: Number in chart is the number of recordkeepers, not a percentage.

## Retirement Income Projection Options Available to DC Plan Participants

Options Made Available by Plan Sponsors (n=214)



Note: Percentages may not add up to 100% due to rounding. Also, the number of plan sponsors represented in this and the following charts exclude one plan sponsor respondent from among the 215 plan sponsors surveyed because that respondent indicated that the company had a DB plan only.

Instead, plan sponsors appear to favor a self-service approach to modeling retirement income projections for their plan participants. Eight in 10 plan sponsors (81%) say that their plan participants have the ability to model how much retirement income they could expect based on their current account balance; nine of the 12 recordkeepers already offer this feature. Unfortunately, however, this “do-it-yourself” model is not taking hold. The majority of recordkeepers surveyed estimated that 25% of plan participants or fewer have made the effort to project their retirement income. This low utilization is in spite of the fact that there appears to be a great deal of flexibility with the current retirement income tools. Nearly all of the recordkeepers surveyed allow participants to input different projected retirement ages, future contributions and interest rate returns. This suggests that parameter flexibility may be far less important than providing a frame of reference that would make engaging with the tools meaningful for participants.

Among the 16% of plan sponsors who say that their participants cannot currently model retirement income projections, one-third say that their recordkeeper does not offer this functionality. However, of the three recordkeepers surveyed who do not currently offer this functionality, two said they plan to offer it in 2012, while the third did not indicate any plans to do so. Additional reasons cited by plan sponsors for not offering income projections included concerns about offering investment advice, as well as fiduciary liability concerns. One plan sponsor expressed a somewhat different concern: they worry that, if permitted to model retirement income, “participants may mistakenly believe that the amount is guaranteed.”

In terms of the assumptions used for modeling retirement income projections, several recordkeepers reported that they provide Ibbotson modeling tools to participants. These typically rely on Monte Carlo simulations and, according to the recordkeepers, include rates made available by the Pension Benefit Guaranty Corporation (PBGC). Half of the recordkeepers reported using more simplistic calculations and assumptions, such as a drawdown strategy, and only one recordkeeper specifically calculates the annuity equivalent value, but was unsure of whether or not the value was based on the PBGC rates or some other industry source.

## RETIREMENT INCOME STRATEGY HIGHLY CORRELATED TO RETIREMENT PLAN FOCUS: WHERE RETIREMENT SAVINGS REMAINS THE PRIMARY FOCUS OF THE PLAN, MOST SPONSORS FAVOR DRAWDOWN STRATEGIES OVER GUARANTEED LIFETIME INCOME, WHILE RECORDKEEPERS APPEAR TO BE SPLIT ON THIS ISSUE

The specific retirement income strategy offered to DC plan participants – either systematic withdrawal payments (SWiPs) or guaranteed lifetime income payments – is strongly correlated to whether the focus of the DC plan is on retirement savings or retirement income.

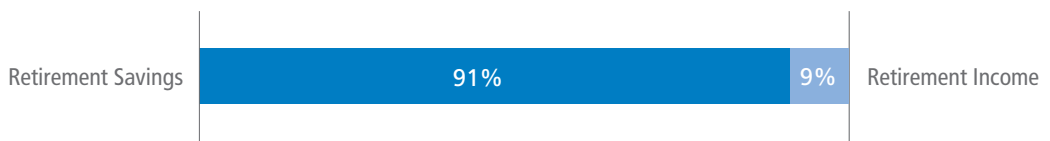
Nearly all plan sponsors (91%) say that retirement savings, rather than retirement income, is still the primary focus of their DC plan(s). Only 9% of plans sponsors surveyed say that retirement income is the primary focus of their DC plan(s). Eleven of the 12 recordkeepers agree, stating that the majority of their plan sponsor-clients view retirement savings as the primary focus of their DC plans today.

### Primary Focus of Defined Contribution Plans:

Retirement Savings vs. Retirement Income

Plan Sponsors' Perspectives of Their Own Plans (n=214)

The primary focus is...



*Changing the retirement plan's ultimate focus from savings to income is a prerequisite for creating the frame of reference necessary for both sponsors to offer, and for participants to select, guaranteed retirement income.*

There is a full complement of retirement income options available in the marketplace today that range from total liquidity (e.g., a drawdown strategy) at one end to guaranteed income (e.g., an annuity) at the other. When plan sponsors were asked which was closer to their own view when they thought about retirement income – systematic withdrawal payments or guaranteed lifetime income payments – 67% of plan sponsors overall think of retirement income in terms of SWiPs and 33% think of retirement income as a guaranteed lifetime income payment (i.e., an income annuity).

### **View of Retirement Income for DC Plan Participants: Systematic Withdrawal Payment vs. Guaranteed Lifetime Income Payment**

Plan Sponsors' Perspectives (n=214)



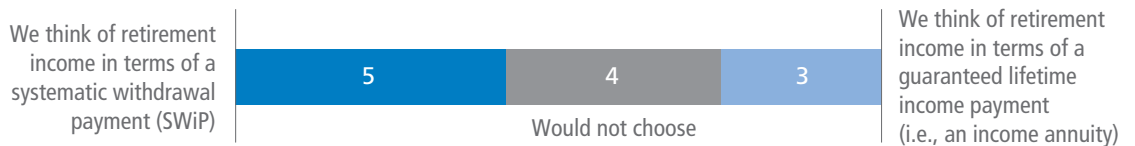
When looking at the specific focus of their DC plan(s), 71% of plan sponsors with retirement savings as a primary focus said they think of retirement income in terms of SWiPs, while 29% think of retirement income as a guaranteed lifetime income payment (i.e., an income annuity). For the small group of plan sponsors who state that retirement income is a primary focus of their plan(s), the opposite is true – 74% think of retirement income as a guaranteed lifetime income payment (i.e., an income annuity) vs. 26% who think of retirement income in terms of SWiPs. This strong correlation suggests that changing the retirement plan's ultimate focus from savings to income is a prerequisite for creating the frame of reference necessary for both sponsors to offer, and for participants to select, guaranteed retirement income.

*When it comes to DC plans, a participant cannot get to a secure retirement without saving enough, regardless of whether the ultimate income stream is taken as an annuity or a SWiP.*

When recordkeepers were asked which was closer to their own view when they thought about retirement income – systematic withdrawal payments or guaranteed lifetime income payments – it was difficult for many of them to choose one over the other. A number of recordkeepers cited that there was a strong place for both strategies, depending on client and participant needs. Additionally, several emphasized that both savings and income are important, and that when it comes to DC plans, a participant cannot get to a secure retirement without saving enough, regardless of whether the ultimate income stream is taken as an annuity or a SWiP.

### **View of Retirement Income for DC Plan Participants: Systematic Withdrawal Payment vs. Guaranteed Lifetime Income Payment**

Recordkeepers' Perspectives (n=12)



Note: Number in chart is the number of recordkeepers, not a percentage.

However, among those recordkeepers that did choose one strategy over the other, SWiPs were selected slightly more frequently than guaranteed lifetime income payments. It is important to note that SWiPs – in which a stream of payments, expressed as a fixed percentage (generally 4%) of the declining portfolio, is paid – expose participants to significant market risk and, as such, do not guarantee that income streams will be paid throughout the lifetime of the payee or for any minimum time period. While these programs have their place in an overall retirement plan, they do not meet the same need as annuities and do not provide guaranteed lifetime income.

## EVEN THOUGH PLAN SPONSORS ARE SPLIT ON WHETHER DC PARTICIPANTS FAVOR LUMP SUMS VS. HAVING A PORTION OF THEIR BENEFITS PAID IN THE FORM OF MONTHLY INCOME, LUMP SUM DISTRIBUTIONS TRUMP OTHER DISTRIBUTION OPTIONS IN BOTH DC AND, WHEN OFFERED, IN DB PLANS

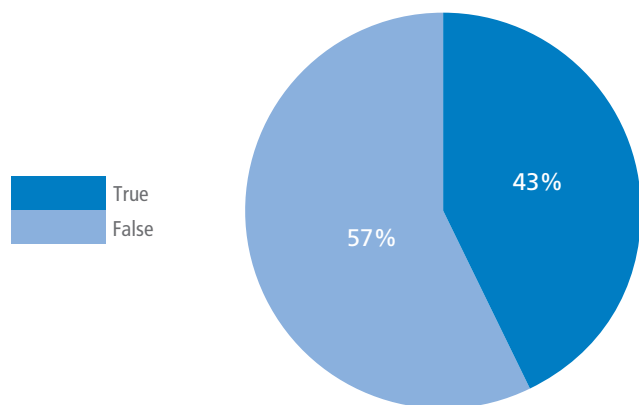
When asked whether or not their participants favor a lump sum distribution from their defined contribution plans over a monthly stream of income, plan sponsors were divided. Four in 10 plan sponsors (43%) agree that when their DC plan participants retire, the majority of these participants would prefer to “receive at least part of their retirement savings as monthly income for as long as they live rather than receiving all of it in a lump sum that they would invest themselves,” while 57% of plan sponsors feel that their plan participants would prefer the lump sum.

### DC Plan Participant Preferences:

#### Lump Sum vs. Part of Retirement Savings as Monthly Income

##### Plan Sponsors' Perspectives (n=214)

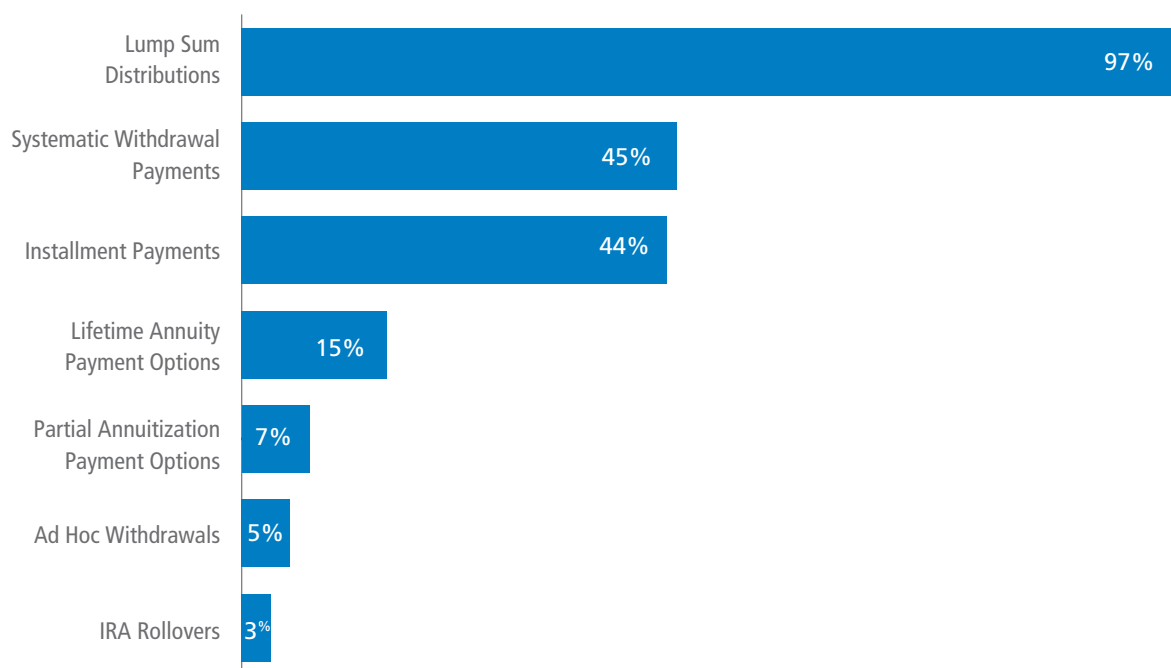
When they retire, the majority of our DC plan participants would prefer to receive at least part of their retirement savings as monthly income for as long as they live, rather than receiving all of it in a lump sum that they would invest themselves.



Even though nearly half of plan sponsors think their participants favor monthly income, lump sum distributions are nonetheless the most widely offered DC plan distribution option – offered by nearly all plan sponsors (97%), followed by SWiPs (45%) and installment payments for a defined period of time (44%).

### DC Plan Distribution Options Offered

Plan Sponsors' Perspectives (n=214)



Among the 97% of plan sponsors who indicated that they offer lump sum distributions from their DC plans, all say they allow for full lump sums – and 57% allow for partial lump sums – to be taken from their company's DC plan. Sponsors who offer a full lump sum said that 81% of participants take the lump sum; sponsors who offer partial lump sums said that 16% of participants take the partial lump sum. Every recordkeeper surveyed said that plan participants were either somewhat or very likely to take a lump sum withdrawal from the plan at the point of retirement, even those who may initially leave their balance in the plan for a couple of years



following retirement. It is important to note, however, that at least some of the recordkeepers do not distinguish between lump sum cash withdrawals and qualified rollovers (e.g., into an IRA or another qualified plan), so this figure includes both.

The findings also point to a trend toward lump sum distributions in DB plans, which were intended to provide guaranteed income throughout retirement – not to provide lump sum distributions that can be depleted before the end of one’s retirement. Lump sum payout options were widely introduced when the economics of prevailing interest rates made lump sum forms of payout significantly less expensive for employers than standard lifetime income forms and, therefore, more attractive to employees. These distributions also helped facilitate the early retirement incentive programs that became widespread in the 1990s, with the result that lump sum payouts financed not lifetime security but rather the transition to early retirement.

Today, half of plan sponsors (54%) who offer DB or hybrid plans say they allow for full lump sum distributions – and 25% allow for partial lump sum distributions – to be taken from their company’s DB or hybrid plan, and every recordkeeper surveyed administers at least some DB plans that offer lump sum distributions. Most of the recordkeepers surveyed were unsure if the majority of these DB plans offer – or if plan participants take – full or partial lump sum distributions. Plan sponsors with DB plans seem to have a clearer indication as to their retirees’ distribution preferences. Sponsors who offer full lump sum distributions said that two-thirds of participants (65%) take a full lump sum; sponsors offering partial lump sums from their DB plans said that 13% of participants had selected this option.

## MANY PLAN SPONSORS BELIEVE PARTICIPANTS WANT GUARANTEES AND LIFETIME INCOME, YET INCOME ANNUITIES ARE NOT WIDELY OFFERED

More than two-thirds of plan sponsors (68%) said they believe the majority of their DC plan participants favor “guarantees that offer stable but somewhat lower returns” over a “higher degree of risk because the returns could be greater” (32%). Additionally, almost half (44%) said that the majority of their DC plan participants would prefer to “receive at least part of their retirement savings as monthly income for as long as they live rather than receiving all of it in a lump sum that they would invest themselves.” However, income annuities, which combine stable returns and guaranteed lifetime income, are rarely offered by plan sponsors.

### Viewpoint of DC Plan Participants:

Guarantees That Offer Stable but Somewhat Lower Returns vs. Higher Degree of Risk Because the Returns Could Be Greater

Plan Sponsors' Perspectives (n=214)

They prefer guarantees that offer stable but somewhat lower returns

68%

32%

They prefer a higher degree of risk because the returns could be greater

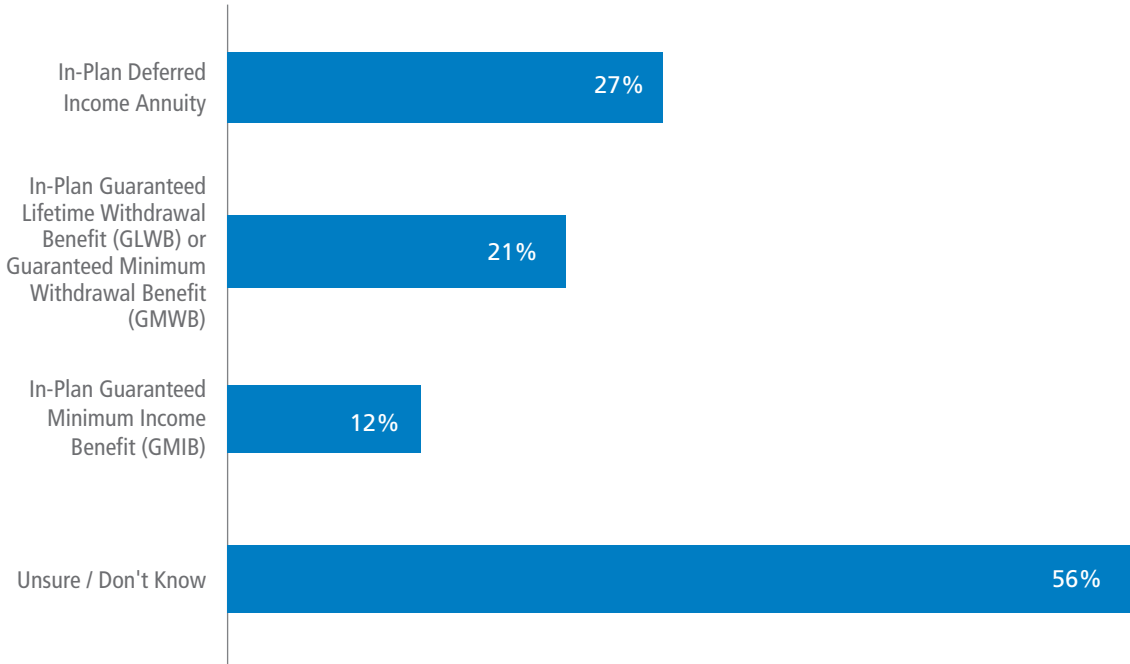
For DC plan participants who are still saving for retirement, there are several types of in-plan accumulation annuity products that are available in the market today, including deferred fixed income accumulation annuities that are available either as stand-alone products or products that can be integrated into target date funds. These products allow a plan participant to dollar cost average into a deferred annuity with a part of their account balance, and at retirement, that portion of the account balance is converted into a guaranteed stream of income for life. There are also living benefit options, including Guaranteed Minimum Income Benefit (GMIB), Guaranteed Lifetime Withdrawal Benefit (GLWB) or Guaranteed Minimum Withdrawal Benefit (GMWB), that are available in either a balanced or a target date fund at a specified age.

Some insurers have introduced a new generation of annuities which offer more flexibility, access to assets, a variety of variable and fixed interest options, and reduced fees. Annuities are sometimes misunderstood because they are incorrectly compared to investment vehicles, even though they are insurance products – with additional risk assumed by the insurer (e.g., mortality, longevity and investment risk). As a result of this comparison, annuities are sometimes thought to be inflexible and expensive – and, therefore, have been overlooked by plan sponsors and recordkeepers as a potential component of a sound retirement portfolio. This new generation of products seeks to overcome these barriers.

Today, only 16% of plan sponsors surveyed offer any form of in-plan systematic retirement income options such as income annuities, managed accounts, payout funds, etc., while DC plan participants are still saving for retirement. Among the 16% of plan sponsors who say they make in-plan retirement income options available to their participants, the most widely offered option appears to be an in-plan deferred income annuity (27%, or 4% of respondents overall). A startling 56% of plan sponsors who said they offer an in-plan retirement income option do not know specifically what type of product is being offered.

### In-Plan Retirement Income Options Offered to DC Plan Participants

Plan Sponsors' Perspectives (DC Plan Offers In-Plan Retirement Income Options, n=34)

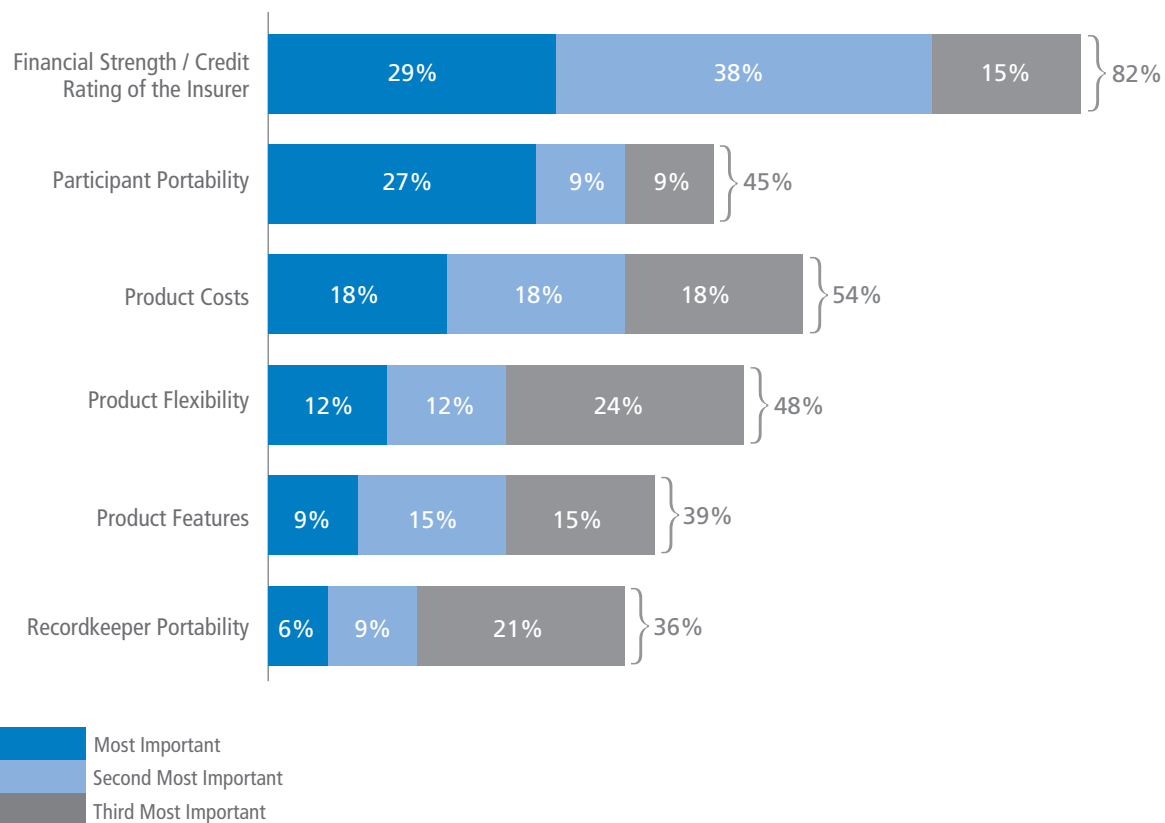


Note: Multiple responses possible.

Among sponsors who report that they do offer in-plan retirement income products, the features cited as the most compelling for offering such products are “protection against longevity risk” (35%) and “annual payments” (21%); the most important criterion for evaluating specific products before deciding which to offer is “financial strength / credit rating of the insurer” cited by 29% of plan sponsors who offer them. That selection was followed closely by 27% of plan sponsors who indicated that the most important criterion for evaluating in-plan retirement income offerings is the portability of guaranteed income when a participant has a distributable event – known as “participant portability” – in the form of a Rollover IRA or as a qualified plan distributed annuity. This differs from “recordkeeper portability” – the portability of the product when the plan sponsor changes a plan recordkeeper.

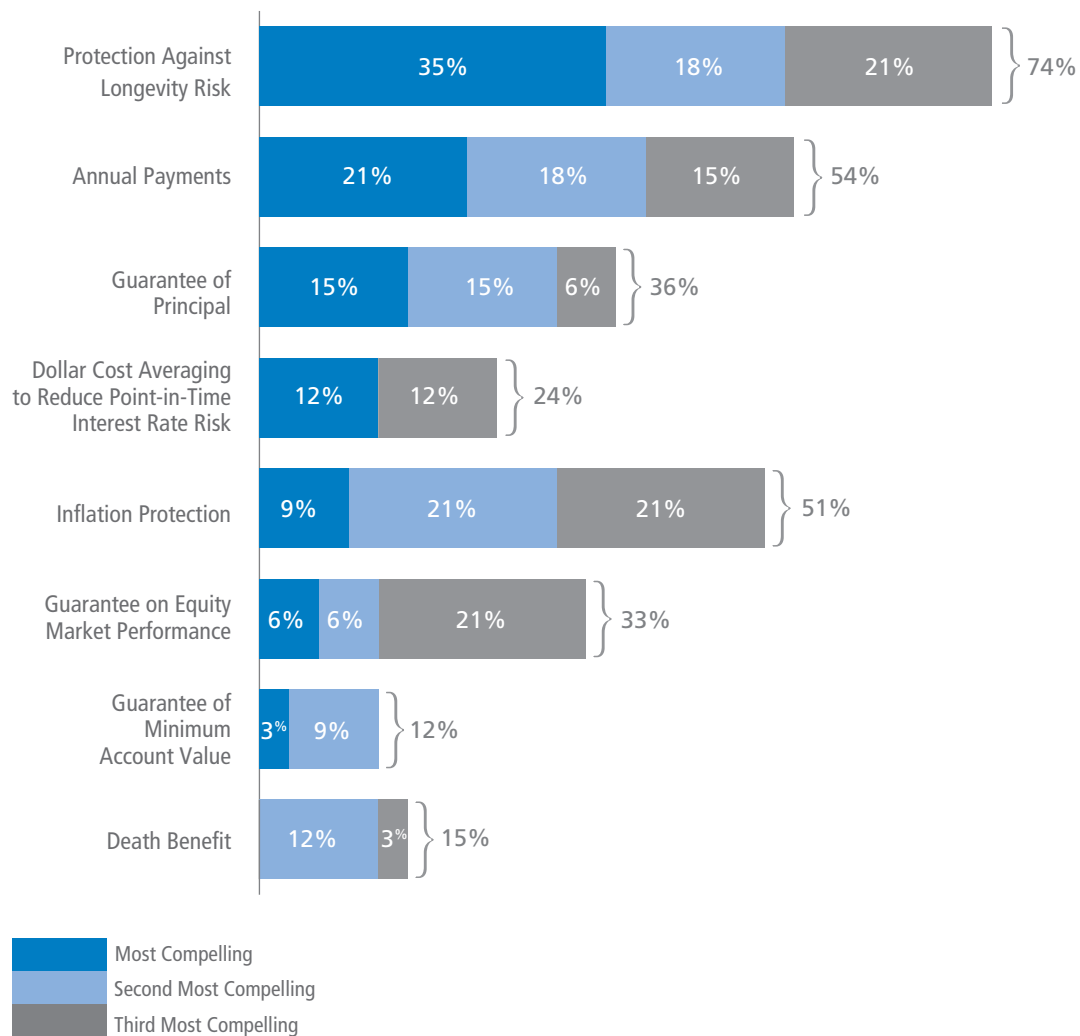
**In-Plan Retirement Income Options:  
Most Important Selection Criteria**

Plan Sponsors’ Perspectives (DC Plan Offers In-Plan Retirement Income Options, n=34)



## In-Plan Retirement Income Options: Most Compelling Product Features

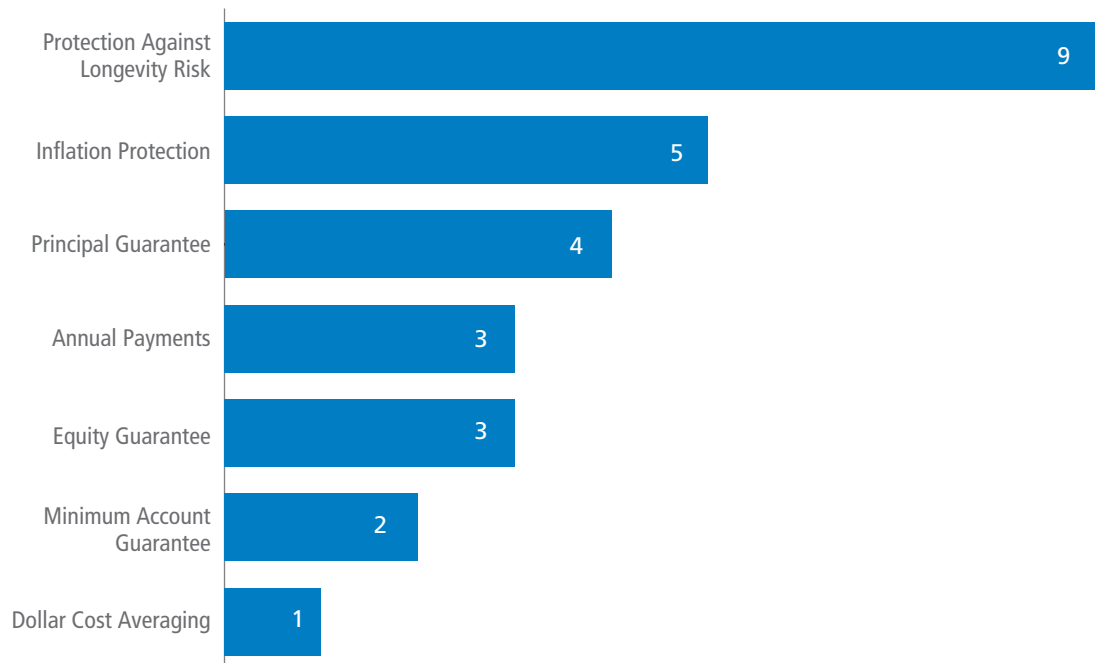
Plan Sponsors' Perspectives (DC Plan Offers In-Plan Retirement Income Options, n=34)



“Protection against longevity risk,” “inflation protection” and “principal guarantee” were selected by recordkeepers as the top three most compelling features for including in-plan retirement income options on their platforms. “Financial strength / credit rating of the insurer,” “participant portability” and “product costs” are recordkeepers’ top three most important criteria for selecting a specific in-plan product.

### **In-Plan Retirement Income Options: Most Compelling Product Features**

Recordkeepers’ Perspectives (n=9)

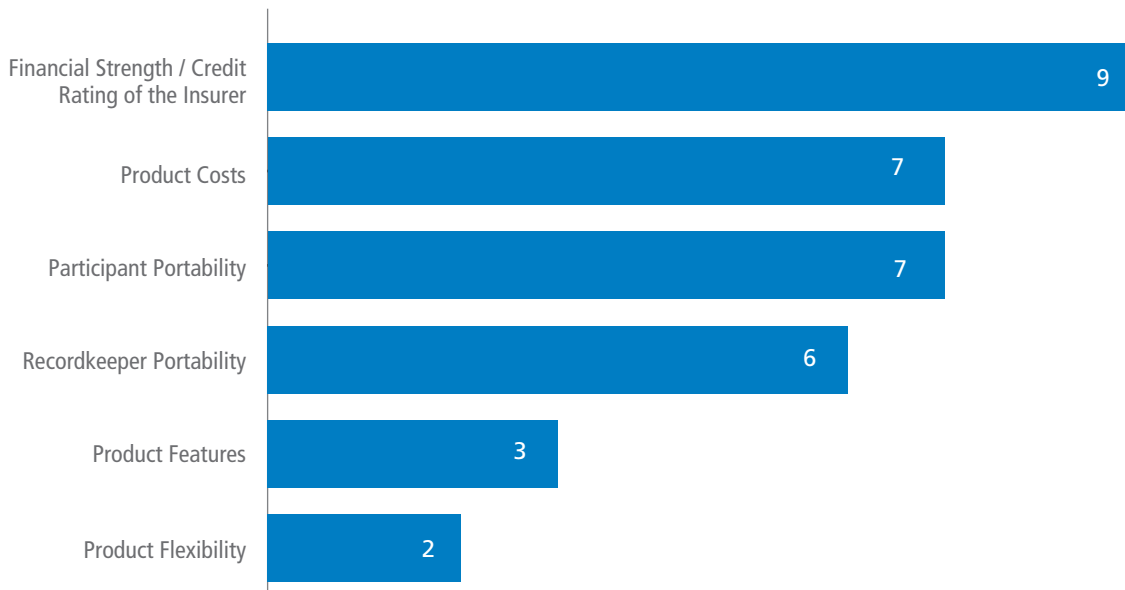


Note: Number in chart is the number of recordkeepers, not a percentage.

## In-Plan Retirement Income Options:

### Most Important Selection Criteria

Recordkeepers' Perspectives (n=11)



Note: Number in chart is the number of recordkeepers, not a percentage.

For retiring workers, fewer than one in five plan sponsors (16%) offer income annuity options at the point of retirement to their DC plan participants. Of the small percentage of plan sponsors who offer an annuity as a distribution option, 71% (or 11% of plan sponsor respondents overall) offer an IRA rollover annuity; 68% (or 11% of plan sponsor respondents overall) offer an immediate annuity; and, 53% (or 8% plan sponsor respondents overall) offer partial annuitization. A much smaller percentage (18%, or 3% of plan sponsor respondents overall) offers longevity annuities, a relatively new type of deferred income annuity that allows a retiree to purchase an annuity at retirement, say age 65, that will be converted into a stream of income at a later date, such as age 85.

One-quarter of plan sponsors (24%) who offer an income annuity at the point of retirement say they offer participants the ability to purchase annuities through the Hueler Income Solutions<sup>®</sup> platform,<sup>9</sup> though not necessarily to the exclusion of being able to purchase it directly through their employer. Half of the recordkeepers said they offer access to the Hueler platform, which many in the industry agree has future potential, yet usage among participants is still very low. As with the previous findings, this suggests that the way in which the qualified retirement plan itself is framed by sponsors is critical to how its participants perceive it and the decisions they make.

## SPONSORS AND RECORDKEEPERS AGREE FIDUCIARY CONCERNS AND PERCEIVED LOW DEMAND PREVENT MORE WIDESPREAD OFFERING OF ANNUITIES IN THE WORKPLACE

Offering income annuities requires plan fiduciaries to prudently select one or more annuity providers. This, as with any qualified plan design or provider selection, is a fiduciary decision. Unlike more established plan design and investment option features which have safe harbors, the annuity provider selection does not, thereby creating potential liability for sponsors. Eight in 10 plan sponsors (79%) say that fiduciary liability concerns are discouraging them from more widespread offering of income annuities within their DC plan(s) – with at least one commenting that their company “tends to shy away from offering options that expose [them] to greater fiduciary liability.” More than half of plan sponsors (56%) also believe those concerns are dissuading their recordkeepers from more widely offering these products on their platforms.

<sup>9</sup> Hueler Income Solutions<sup>®</sup> allows participants to purchase institutionally priced annuities from their choice of insurers on the platform. Each annuity quote provided by the participating insurance companies is offered to individuals on a group or institutional price basis, due to the volume and buying power represented by all the large companies combined who utilize the Income Solutions<sup>®</sup> program. This may result in an annuity with higher monthly income payments to the individual. Income Solutions<sup>®</sup> is not available to the general public. It is available only to individuals whose recordkeepers/service providers, benefit consultants, corporate plan sponsors and advisors have partnered with Income Solutions<sup>®</sup> [www.incomesolutions.com](http://www.incomesolutions.com).

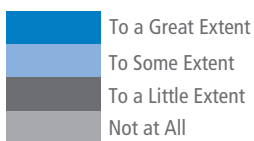
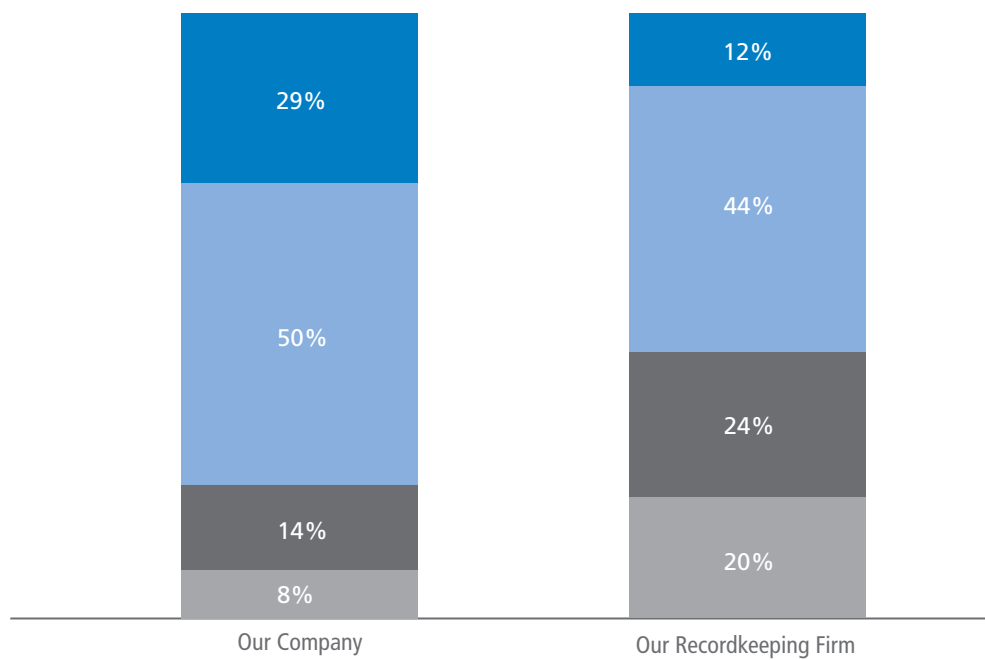


*The way in which the qualified retirement plan itself is framed by sponsors is critical to how its participants perceive it and the decisions they make.*

### Extent to Which Fiduciary Liability Issues Are Preventing More Widespread Offering of Income Annuities in DC Plans:

By Companies vs. Recordkeepers

Plan Sponsors' Perspectives (n=214)

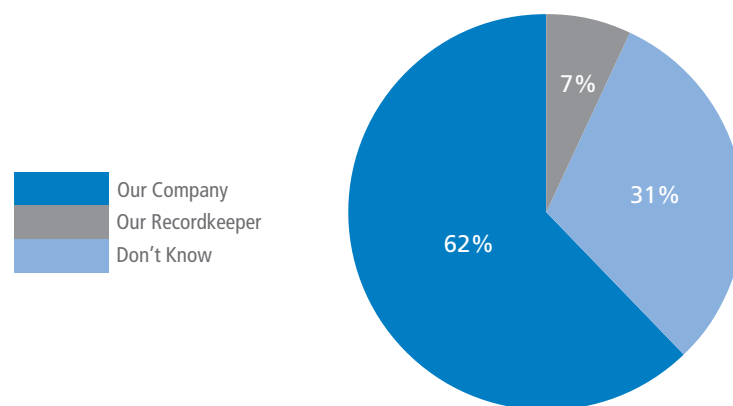


Note: Percentages may not add up to 100% due to rounding.

Interestingly, most plan sponsors (62%) believe that their company is more concerned about annuity-related fiduciary liability issues than their recordkeeper; only 7% of plan sponsors believe their recordkeeper is more concerned, and 31% say they don't know who is more concerned.

### **Annuity-Related Fiduciary Liability: Who is More Concerned?**

Plan Sponsors' Perspectives (n=214)



The recordkeepers unanimously agree: plan sponsors are much more concerned about fiduciary liability issues than they are. The recordkeepers believe there are several reasons for this – the primary one being that plan sponsors are very conscious of their fiduciary responsibilities. Recordkeepers believe plan sponsors are “waiting for the Department of Labor to issue fiduciary safe harbor guidance” and they are “somewhat unlikely to add these [products] unless there is a regulatory change that provides the plan sponsor with some fiduciary protection.” Absent that action from the Department of Labor, they may not want the added responsibility of choosing an annuity provider.

*One recordkeeper admitted that they recently had a plan sponsor client who threatened to leave its platform if they did not make a retirement income option available to their participants.*

Other reasons cited by recordkeepers as preventing more widespread offering of income annuities: low level of interest by plan sponsors; perceived confusion over product features; and, a belief by several recordkeepers that advisory services, including the recordkeepers' own propriety services, were more appropriate solutions for participants. Despite these perceived barriers, some plan sponsors said that income annuities are not offered because they are not available on their recordkeeper's platforms, and one recordkeeper admitted that they recently had a plan sponsor client who threatened to leave its platform if they did not make a retirement income option available to their participants.

## THERE IS INCOMPLETE UNDERSTANDING AMONG PLAN SPONSORS ABOUT THEIR RECORDKEEPERS' RETIREMENT INCOME COMMITMENT, CAPABILITIES AND OFFERINGS

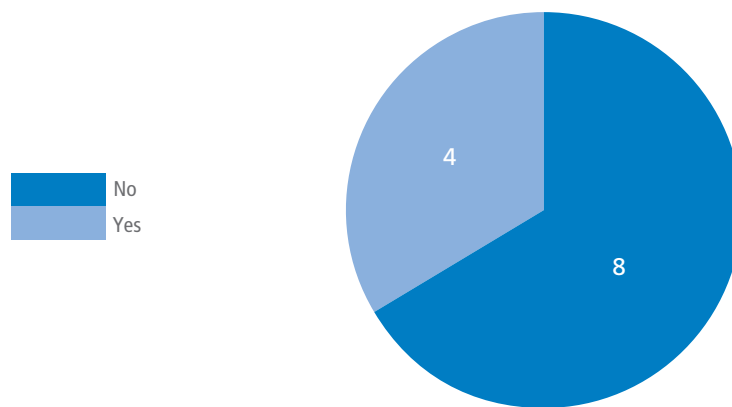
Even though recordkeepers point to plan sponsors' low level of interest as one of the primary reasons that there is not more widespread offering of retirement income products to plan participants, this may be painting an incomplete picture, because there also appears to be an incomplete understanding on the part of some plan sponsors as to the retirement-income commitment, capabilities and offerings that are available from their recordkeepers.

The majority of recordkeepers do not make institutional income annuities and other retirement income products available at the point of retirement, nor do they have the ability to administer in-plan accumulation annuity options. In fact, the availability of in-plan retirement income options among recordkeepers is still relatively low, with only four of the 12 recordkeepers currently offering them. However, of the eight recordkeepers who do not currently offer an in-plan option, four said they are very likely to devote the resources to build the infrastructure required for in-plan retirement income options to be available on their platforms in the next 18 months. According to those recordkeepers who state that they do not currently offer in-plan retirement income options and are not planning to devote the resources in the foreseeable future to an infrastructure build, there is low demand from plan sponsors and their participants, with one recordkeeper commenting that they are "not going to build anything until someone wants to offer a product."

## Ability for In-Plan Accumulation Annuities and Other Retirement Income Products to Be Offered On Recordkeeper's Platform

Recordkeepers' Perspectives (n=12)

Do you currently offer an in-plan retirement income option to plans on your platform?



Note: Number in chart is the number of recordkeepers, not a percentage.

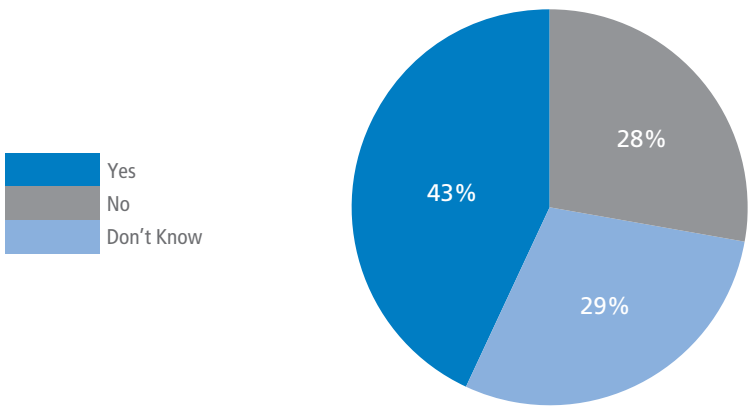
While some recordkeepers offer or may be considering offering these options on their platform, nearly one-third of plan sponsors (29%) do not know whether their recordkeeper's platform currently allows for in-plan accumulation annuities and other retirement income products to be offered to their DC plan participants. Additionally, among the 28% of plan sponsors who said that their recordkeepers do not currently offer these products on their platforms, one-quarter (22%) are unsure about the likelihood of their recordkeeper building the infrastructure for in-plan accumulation annuities and other retirement income products in the next 18 months.

Nearly one-third of plan sponsors do not know whether their recordkeeper's platform currently allows for in-plan accumulation annuities and other retirement income products to be offered to their DC plan participants.

### Ability for In-Plan Accumulation Annuities and Other Retirement Income Products to Be Offered On Recordkeeper's Platform

Plan Sponsors' Perspectives (n=214)

Does your recordkeeper currently offer an in-plan retirement income option to plans on its platform?



Some have a clearer sense of their recordkeeper's intentions. Nearly half of plan sponsors (47%) believe their recordkeeper is very or somewhat likely to build the infrastructure to offer these products, but one-third (32%) believe they are somewhat or very unlikely to do so. For those who think it is likely to happen, 64% believe their recordkeeper would be the one to incur the majority of the costs related to building the infrastructure, while 25% believe it would be passed along to the recordkeepers' clients. Like the recordkeepers, some plan sponsors cite "not enough plan sponsor interest in these types of product," and it is perceived as "too expensive to build and to pass the cost on to the plan sponsor." At least one said they "have never heard [their recordkeeper] discuss this issue."

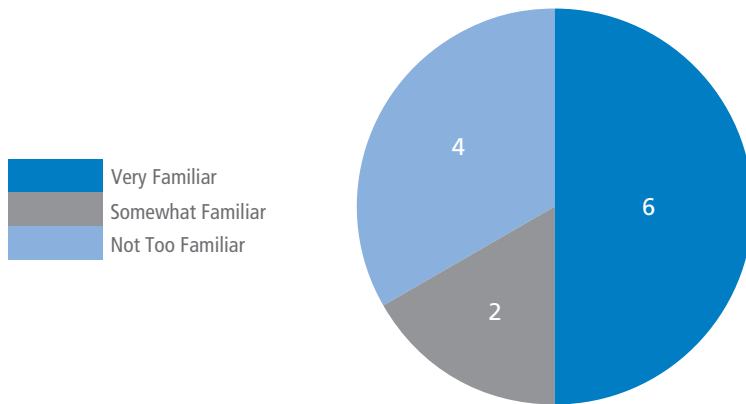
## INDUSTRY RETIREMENT INCOME DATA STANDARDS, WHICH MOST RECORDKEEPERS ARE COMMITTED TO ADOPTING, HAVE LOW AWARENESS AMONG PLAN SPONSORS

Over the past few years, recordkeepers – in partnership with retirement income providers – have made strides in working to facilitate industry standards for the new generation of in-plan retirement income products offered in employer-sponsored retirement plans. Data Layouts were developed by The SPARK Institute<sup>10</sup> in order to facilitate uniform expectations among retirement income product providers and recordkeepers who decide to offer these products and solutions in employer-sponsored retirement plans.

All recordkeepers surveyed were aware of The SPARK Institute’s protocols for Data Layouts for Retirement Income Solutions for in-plan options, which were released in 2010. However, their level of familiarity with the protocols varied. Six recordkeepers said they were very familiar, two

### Familiarity with SPARK Institute’s Protocols for Data Layouts for Retirement Income Solutions

Recordkeepers’ Perspectives (n=12)



Note: Number in chart is the number of recordkeepers, not a percentage.

<sup>10</sup> The SPARK Institute, Inc., *Data Layouts for Retirement Income Solutions*, September 30, 2010.

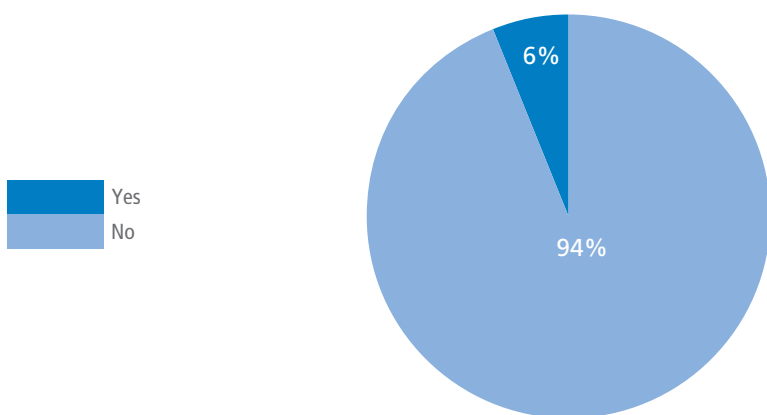
recordkeepers said they were somewhat familiar and four recordkeepers said they were not too familiar – none of the latter four currently offer in-plan retirement income products.

Six of the eight recordkeepers who offer, or said they plan to offer, in-plan annuity products have either adopted and implemented the protocols or said they plan to do so within the next 18 months. The remaining two recordkeepers said they are somewhat unlikely to adopt and implement the protocols.

It was very interesting to note that when plan sponsors were asked if they were aware of the protocols, 94% of them said they were not. Of the small percentage who were aware of them, the large majority said they were only “somewhat familiar” (42%), “not too familiar” (42%), or “not at all familiar” (8%), and many of those who were aware of the protocols were “unsure” as to whether or not their recordkeeper had adopted (67%) or implemented (50%) the protocols.

### Awareness of SPARK Institute’s Protocols for Data Layouts for Retirement Income Solutions

Plan Sponsors’ Perspectives (n=214)



## RETIREMENT INCOME IS EXPECTED TO EMERGE AS ONE OF THE BIGGEST RETIREMENT PRACTICES TRENDS IN THE FUTURE

Looking ahead, both plan sponsors and recordkeepers believe that a focus on retirement income will be one of the biggest retirement practices trends to emerge in the next three to five years. About one-third of plan sponsors agree with this prediction, which garnered more attention among this group than any other future trend that is expected to emerge.

One plan sponsor noted that they believe “lifetime income will gain traction within DC plans and will be the biggest retirement trend over the next five years,” while others echoed this sentiment by commenting that “there will be a greater concentration on retirement income” and there will be “more of a shift from a retirement savings focus to a retirement income focus.” Coming nearly full circle to recognize the importance of guaranteed retirement income, another believes that there will be a move to figure out “how to make a DC plan look and feel like a DB plan.”

Other plan sponsors were more specific in their predictions about how retirement income may take hold. One predicted that companies will “start to offer more guaranteed income options such as annuities again” and another believes there will be “greater concentration on...annuity-type distributions.” Still another plan sponsor went so far as to say that “[government] mandates are expected for the annuitization of [retirement plan] account balances.”

For recordkeepers, their expectations are even more sanguine. Nearly all – 10 of the 12 – recordkeepers surveyed said an increasing focus on retirement income is among their top predictions for the next three to five years. Some predict that “there will be increasing focus on retirement income” and the “shift to retirement income will continue to come to the forefront as sponsors will increasingly view the retirement benefit from the income lens,” while another believes “the shift in focus from accumulation to income streams is definitely starting.” One believes that the advisor community will play an important role and “will make changing the dialogue from accumulation to retirement income their number one priority.”



Notwithstanding the prediction by one plan sponsor that retirement income solutions may be mandated in the future, at least one recordkeeper believes that “there will be a key focus on retirement income information, whether mandated or not.” Regardless of how the industry gets there, there is a growing recognition that having participants “target a particular number or savings rate is not the answer.” Rather, participants “need to be presented with their projected monthly income and asked ‘Can you live with that?’”

While there was not consensus among the recordkeepers in terms of the specific products that might be offered (or the manner in which they will be made available to plan participants), income annuities, including longevity insurance, are among the retirement income products that are expected by recordkeepers to be included among the lineup as are products that are “annuity-like with more flexibility.” A lack of consensus about the specific products that may be offered appears to be tied to some uncertainty about how the regulatory environment will take shape for these products. One recordkeeper summed it up by saying that “regulation will dictate the direction and types of products” that will emerge with the hope that those in the industry “will have the ability to shape or influence that [regulation].”

# Conclusion

Those who manage qualified retirement plans appear to be at an important crossroads in the evolution of these workplace benefits. At this juncture, plan sponsors and their recordkeepers may find themselves trying to decide whether the primary plan objective is – or should be – retirement savings or retirement income. While the two objectives certainly intersect, in the former, retirement savings is the end goal; in the latter, retirement savings is a means to the goal of retirement income. For any given plan, one will likely dominate, and it is the dominant objective that will likely drive future decisions about plan design, education and product offerings. It may also impact the extent to which these groups try to influence regulatory and industry developments.

If a focus on retirement income takes hold, as many in the industry predict, then there is a range of considerations for plan sponsors and recordkeepers. While they may not apply equally to all plan sponsors and recordkeepers, these suggestions – outlined in the Call to Action section on the following pages – should be given careful consideration. They will almost certainly have a significant influence over how plan participants see their choices and create the frame of reference for most plan participant decision making.

## CONSIDERATIONS FOR PLAN SPONSORS

### **Plan Sponsors Should Recognize That Reframing Their Qualified Plans From a Savings Focus to an Income Focus May Be the Most Important First Step to Take**

Nearly all plan sponsors and recordkeepers believe that retirement savings, rather than retirement income, is still the primary focus of DC plans. And, for the small majority who believe retirement income is the primary focus, many are finding it difficult to translate their intentions into action. Some DB plans, which were designed to provide guaranteed lifetime income, appear to be moving away from that form of benefit. Still, reframing qualified plans to focus on income rather than savings is a critical and necessary first step to creating a culture of retirement income. Until plan participants' mindsets shift from assets to income, they are not likely to take the steps to determine their retirement income needs, nor are they likely to take advantage of the lifetime income options that are made available to them in the workplace. Put another way, only if the plan's frame of reference is income will participants tend to see their choices in those terms and make elections accordingly.

### **Plan Sponsors Should Provide Options to DC Plan Participants That Will Help Them Convert a Portion of Their Retirement Savings into Guaranteed Lifelong Income**

For most workers, retirement will be funded, completely or in significant part, by DC plans. Therefore, it makes sense that options should be made available in the workplace for creating lifetime income from these plans. Without these options, as is illustrated by current outcomes, participants may not be able to, on their own, achieve retirement security.

It may help to keep concerns about fiduciary liability relating to selecting providers for specific income generating products in perspective, and recognize that this selection is similar to other provider selections routinely made by the sponsor. Plan sponsors are well positioned to follow a consistent and reasoned due diligence process and select a suitable high quality insurance company to provide annuity benefits to their participants.

When contemplating which retirement income options to offer, plan sponsors and their recordkeepers should decide whether they want to structure their approach as an accumulation option within the plan, a distribution option at the point of retirement, or both. While the distribution option may appear easier to implement, it has historically been challenging to steer

retiring employees away from lump sum distributions, which requires overcoming the “illusion of wealth” effect documented in numerous behavioral research studies.<sup>11</sup>

Plan sponsors should also consider offering partial annuitization from a DC plan at the point of retirement. Another option would be for plan sponsors to consider earmarking their employer match to help participants create a partial guaranteed income stream. From the individual’s perspective, purchasing an annuity with a portion of their assets, instead of converting their entire DC balance into an annuity, can help them generate guaranteed income with just a portion of the balance. This would allow participants to meet basic expenses with the protection of guaranteed income for the future, while being able to maintain flexibility and liquidity with their remaining assets.

#### **Plan Sponsors Should Not Lose Sight of the Original Intent of DB Plans**

When considering distribution options for participants, those employers that still offer a DB plan should remember the original purpose of these plans: to provide a benefit that ensures guaranteed income for life. To carry through on the promise of guaranteed income for life, they may want to consider how lump sum benefit options are communicated. If lump sums are offered, plan sponsors may want to consider adding partial annuitization programs and limiting lump sums from their DB plan(s) to no more than 50% of the account balances. In addition, where plan sponsors have both a DB and a DC plan, it makes sense to consider how each plan’s focus, education, communication and provisions coordinate in practice.

## CONSIDERATIONS FOR RECORDKEEPERS AND PLAN SPONSORS

#### **Recordkeepers and Plan Sponsors Should Recognize Their Role to Educate Their Workers About the Importance of Retirement Income That Lasts a Lifetime**

Since much of today’s workforce will not be able to rely on the guaranteed income that has historically come from traditional DB pension plans, they will have to find ways to make the savings they have accumulated within a DC plan last a lifetime. As we noted earlier in the report, recent surveys have shown that many plan participants worry about outliving their retirement money. Plan sponsors are in the best position to show employees how they can achieve a financially secure retirement.

A first important step toward this goal is making sure participants understand why the calculators and other modeling tools that are made available to them are important, and how to use them,

<sup>11</sup> Miller, Mark. *The Hard Times Guide to Retirement Security*. Hoboken: Bloomberg, 2010. 42.

so they can understand how their retirement savings will translate into income. Proposed rules requiring that plan sponsors and recordkeepers automatically provide these calculations as a standard feature on participant statements, and when account balances are viewed online, may be very important in this regard. In the absence of such rules being finalized, sponsors and recordkeepers should consider taking this step voluntarily, reinforcing the intent of the plan and providing a very helpful perspective to participants in preparing for retirement.

### **With Retirement Income Expected to Be the Biggest Retirement Practices Trend to Emerge in the Near Future, Recordkeepers Should Make Retirement Income Discussions a Priority With Their Plan Sponsor-Clients**

Low awareness among plan sponsors about the retirement income products their recordkeepers offer may signal to recordkeepers that they have an opportunity to discuss with their plan sponsor-clients their strategy for providing retirement income options. They also appear to have an opportunity to educate their clients about the range of solutions currently available in the market and on their platforms, including explaining product specifics, such as features and fees.

### **Recordkeepers and Plan Sponsors Should Discuss Recent In-Plan and Distribution Product Innovations and Address Any Questions About These Products**

Over the past five years, there have been many innovative retirement income products introduced for workplace retirement plans, including in-plan income annuities and managed payout strategies. As plan sponsors and recordkeepers are devising their strategy to offer lifetime income to plan participants, they should familiarize themselves with the range of new in-plan and distribution offerings available in the marketplace.

To address any questions about how these products work, sponsors and recordkeepers should reach out to insurers and financial services firms to meet with them to explain their offerings.

### **If Recordkeepers Are Planning to Implement Standards Such as the SPARK Institute Protocols, They Should Share That Information With Their Plan Sponsor-Clients**

Many recordkeepers have been hard at work with The SPARK Institute to establish, adopt and implement standards that will make it easier and more cost effective for recordkeepers and insurance carriers to make retirement income solutions available to plan participants. According to The SPARK Institute, the standards “will allow customer-facing record keepers to offer one or more products from unaffiliated insurance carriers; will facilitate portability of products when a plan sponsor changes plan record keepers (record keeper portability); and will support portability

of guaranteed income when a participant has a distributable event in the form of a rollover to a Rollover IRA or as a qualified plan distributed annuity (participant portability).<sup>12</sup>

Recordkeepers should discuss these standards with their plan sponsor-clients and explain to them how the standards can benefit plan sponsors and their participants.

## PUBLIC POLICY CONSIDERATIONS

### **Plan Sponsors and Recordkeepers Should Familiarize Themselves with the Recent Treasury Guidance**

The Obama Administration, through its Middle Class Task Force, has supported the promotion and availability of lifetime income products. In 2010, the Department of Labor's Employee Benefits Security Administration, in conjunction with the Department of the Treasury, issued a Request for Information asking for ideas on how to help reduce the chances that workers will run out of funds during their retirement years, for which they received a significant number of responses.

On February 2, 2012, the Treasury Department and Internal Revenue Service released a package of proposed regulations and revenue rulings on guaranteed lifetime income options. The Treasury Department calls the package the "first step in clearing the way for better and more accessible retirement income options."<sup>13</sup> Plan sponsors and recordkeepers should familiarize themselves with this guidance and assess what administrative changes or plan amendments might be needed, should they decide to implement changes that the new rules or regulations, when final, may make possible. They should also give some consideration about how best to communicate with plan participants about any new offerings they may make available as a result of this new guidance.

### **Plan Sponsors and Recordkeepers Should Continue to Voice Their Concerns About the Lack of a Fiduciary Safe Harbor**

As a practical matter, it appears clear that fiduciary concerns must be addressed by public policymakers before income annuities will take hold as a primary feature of DC plans. While clarifying the fiduciary selection regulation is not a panacea, it would go a long way in encouraging more widespread offering of income annuities in DC plans.

<sup>12</sup> The SPARK Institute, *The SPARK Institute Releases Final Data Standards For Lifetime Income Solutions In Retirement Plans*, September 30, 2010.

<sup>13</sup> U.S. Department of the Treasury, February 2, 2012.

# Methodology

The Retirement Income Practices Study<sup>SM</sup> was conducted in two phases between October 2011 and January 2012.

In Phase I, the qualitative phase, MetLife commissioned RG Wuelfing & Associates, Inc. to conduct phone interviews with 12 defined contribution plan recordkeepers that service primarily FORTUNE 500<sup>®</sup> companies.\* The interviewees included executive- and senior-level managers with decision-making authority and subject matter expertise. The interviews were conducted from mid-October to mid-November 2011.

In Phase II, the quantitative phase, MetLife commissioned the research firm MMR to conduct an on-line survey with plan sponsors of retirement plans in cooperation with Asset International. All participants in the study have substantial influence in the decision-making process regarding their company's retirement benefits policy and plan design; half of them are either the final decision maker or make formal recommendations to senior management. In addition, respondents had to be knowledgeable about the plan design and policy offered to their company's U.S. employees. Finally, participants had to work for a company that offered a DC, DB, or cash balance/hybrid plan. A total of 215 plan sponsors participated in the survey, including 113 from FORTUNE 1000<sup>TM</sup> companies.\* All 215 plan sponsors work for companies that offer a DB and / or DC plan, including 148 which offer both a DC and some type of DB plan. Phase II was conducted between December 14, 2011 and January 30, 2012.

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