



A New Income-Generating Option for DC Plans



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To help ensure participants have the potential for some degree of steady income during their retirement years, a potential solution is to encourage plan sponsors to offer managed payout funds (or other income-generating product) on plan menus.

The Challenge

Current 401(k) products do not provide for income distribution in retirement and people are still not adequately prepared to manage retirement expenses. According to EBRI's 2015 Retirement Confidence Survey, only 48% of workers have tried to estimate how much money they would need to save to have a comfortable retirement, and only 45% have estimated the amount of income they would need each month in retirement.

People are also increasingly dependent on employer-sponsored retirement savings plans to fund their retirement income. 74% of workers expect to receive income from an employer-sponsored retirement savings plan. Additionally, only 9% of workers are very confident that Social Security will continue to provide benefits equal to the benefits received by retirees today.

On top of being uncertain about how much income is needed to live on, translating a lump-sum “nest egg” in one’s 401(k) plan into a monthly stream of income during retirement adds an additional level of complexity to the retirement challenges retirees (and pre-retirees) already face. Additionally, while a retiree might have enough income to cover basic expenses in retirement, some might appreciate a way to supplement retirement income in order to maintain their desired lifestyle in retirement. Retirees who want to continue to benefit from institutional pricing and oversight in a 401(k) plan are not able to do so without the availability of income-generating products in the plan.

Proposed Solution

Encourage plan sponsors to adopt income-generating products in 401(k) plans through solutions such as managed payout funds. Managed payout funds can offer a relatively low-cost, lower-risk solution to translating 401(k) plan retirement savings into a stream of income during retirement years.

These funds generally pose fewer fiduciary, regulatory, and administrative concerns than annuities, lifetime retirement/longevity insurance, and/or installment plans (a plan feature that allows for plan sponsors to pay out 401(k) savings to participants in installments during retirement rather than in a lump sum).

Managed pay-out funds come in different varieties and employ different investment philosophies, depending on the plan and participant preferences or needs. For example, fund distributions can be tied to market interest rates, aim to target a constant monthly/annual distribution rate, or provide more assurance to plan participants.

Assumptions and Implementation Steps

First, we need to target pre-retirees. Retired participants (or individuals close to retirement) are likely to already be drawing on other sources of retirement income (e.g., Social Security).

Second, participant communications will be key. Targeted and detailed participant communications when introducing and/or rolling this feature out is important, to avoid any surprises or confusion among plan participants.

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