United Technologies leads the way in terms of lifetime income.

June 15, 2017

MarketWatch Blog by Alicia H. Munnell

Alicia H. Munnell is a columnist for ***MarketWatch*** and director of the Center for Retirement Research at Boston College.

The company has made lifetime income the default option within its target date fund.

United Technologies Corporation is the first major company to offer a secure lifetime income default option within their defined contribution plan. In 2010, UTC closed its cash balance defined benefit (DB) plan to new hires (after closing a traditional DB plan in 2003), but wanted to make its defined contribution plan function more like a DB plan. The management rejected the old savings-and-investment approach and decided on three principles for the plan: 1) keep costs low; 2) keep it flexible; and 3) ensure that participants will have adequate income in retirement.

The company elected an AllianceBernstein Lifetime Income Strategy. This product is an individual target date account with an optional guaranteed minimum benefit. The withdrawal amounts are set to last throughout a participant's retirement, even if the market falls or the account's assets run out. The individual has access to the market value at all times.

The company viewed this approach as the best compromise between an immediate fixed annuity, which would have provided the highest level of income, and a systematic-withdrawal plan, which would have ensured the greatest level of liquidity.

Participants younger than age 48 are defaulted into a target-date fund comprised of a mix of stocks and bonds. Then, at age 48, allocations to the secure income portfolio begin and gradually increase until age 60, at which point a participant is 100 percent allocated to this portfolio.

Insurance companies are then invited each year to bid on the amount they could provide in annual income out of that year’s contributions to the lifetime income portfolio. Once the bids are accepted, the guaranteed income from the year’s contributions is locked in. This process is repeated each year.

The fees are about 15 basis points for those under age 48; rising to around 125 basis points by age 60 for those allocating 100 percent of their assets to lifetime income; and 125 basis points after retirement.

The Lifetime Income Strategy (LIS) provides employees with the minimum dollar amount that they are guaranteed in retirement. If they view that number as too high or – more likely – too low, they can adjust their saving accordingly.

UTC decided to make the LIS the default because people tend to under-estimate how long they will live and thus are reluctant to buy insurance against living too long. The company concluded that insuring against longevity risk was probably right for the vast majority of its employees. Participants, however, have the freedom and control to opt out if they decide it isn’t for them.

Communications are age-based and personalized, triggered as participants reach certain milestones in their lifecycle. URC characterized the communications as “Hey, you’re enrolled in LIS. At the beginning of this year you’re going to start securing guaranteed income. The fees will go up in return for these guarantees, but so will the value of the benefits.” If an employee isn’t in LIS, there’s a communication that says, “Hey, we noticed you’re not in it, and you’re now at the point where you would start to secure guaranteed income. You might want to see if this makes sense for you.”

The program appears to be popular. Why haven’t other companies followed?