Combining a Guaranteed Minimum Withdrawal Benefit with a QDIA

EBRI Policy Forum: 
Decumulation / Retirement Income in Defined Contribution Plans

Mark J. Foley, CFA 
Vice President, Innovative Simplicity 
Prudential Retirement

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Delivering Positive Outcomes: What is the Right Target?

Investment Dilemma

Upside Potential: Protecting against outliving your money?

Protecting Retirement Income from Market Drop?

Participant’s Lifecycle

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Delivering Positive Outcomes: Possible Through Asset Allocation Alone?

- Growth of retirement assets
- Accumulation
- Transition: Retirement readiness
- Lifetime income

**Market drop:** Reduce expected withdrawal or delay retirement? Guarantee basis for income, even if the market drops

**Market drop:** Reduce withdrawal or return to work? Stable withdrawals guaranteed, even if the market drops

Will you outlive your money? Lifetime income, guaranteed

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How Guarantees Could Improve Target Date Funds’ Risk/Return Trade-Offs

“Typical” Target Date Fund Family

Typical target date funds – without guarantees – try to address volatility risk by increasing bond allocations and thereby lowering long-term expected returns in retirement.

Years Before/After Target Date

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How Guarantees Could Improve Target Date Funds’ Risk/Return Trade-Offs

“Typical” Target Date Fund Family
Typical target date funds – without guarantees – try to address volatility risk by increasing bond allocations and thereby lowering long-term expected returns in retirement.

“Improved” Glide Path with Guarantees
Since income guarantees address the “downside” of poor or volatile markets reducing retirement income, fund managers can employ asset allocations with higher long-term expected returns.

Note: Fund allocations assume the current year is 2009 or 2010

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Establishing an “Income Base” Provides a Guaranteed Basis for Income

Guaranteed return of transfers and contributions is included in the Highest Birthday Value.

- **Highest Birthday Value (HBV)**
  Guarantees potential to capture market upswings by comparing current Market Value against previous years. If higher, the Highest Birthday Value is reset.

- **Market Value**
  of the target date funds when participants start taking guaranteed withdrawals.
Stable Income Guaranteed, as Withdrawals from the Target Date Fund

Guaranteed lifetime withdrawals will be based on age:

- 4.25% beginning at age 55
- 5.00% beginning at age 65
- 5.75% beginning at age 70

* If participants begin withdrawals from age 55 through age 64, their withdrawals will be based on a lower percentage of their Income Base. If participants begin withdrawals after age 70, their withdrawals will be based on a higher percentage of their Income Base.
Positive Market Performance Can Increase Annual Guaranteed Income

If the market value of the target date fund exceeds the Income Base on any of the participant’s birthdays, the withdrawal amount will increase.
Lifetime Income, Guaranteed, Even if Withdrawals Exhaust Market Value

Even if investment performance and guaranteed withdrawals bring the market value to $0, checks will continue and never decrease
Additional Items to Consider

- No annuitization: lifetime income does not require an irrevocable commitment

- Basic operation like any other plan investment option
  - Invest by allocating contributions or transferring existing balances
  - Can take money out at any time by initiating a transfer or withdrawal

- Ability to withdraw more or less than the Lifetime Annual Withdrawal Amount each year
  - “No rollover minutes”: Untaken amounts do not carry over to future years
  - Excess Withdrawals reduce future Lifetime Annual Withdrawal Amounts proportionately

- Optional spousal benefit

- Minimum distribution “friendliness”

- Plan sponsor “portability”: Available on multiple record keeping platforms

- Additional protection does come at an additional cost
  - Cost = investment management fee + guarantee fee
  - Guarantee fees only apply when guarantees are “active”
Numerical Examples
IncomeFlex Illustration A (Accumulation)

**Assumptions**

- Current Age: 50
- Initial Transfer: $100,000
- Retire Age/Status: 65 Single
- Biweekly Contribution: $100
- Market Condition: Up 7.56% (Accumulation) – Up 7.98% (Payout)
- Guarantee Fee: 100bp
- Management Fee: 63bp

**Values at Lock-In age 65:**

- Highest Birthday Value: $330,500
- IncomeFlex Market Value: $299,710
- Zero Return Market Value: $113,000

This is a hypothetical illustration of how IncomeFlex might work and is not meant to represent the performance of any specific investment option. For illustration purposes all numbers have been truncated. It is possible to lose money investing in securities.

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IncomeFlex Illustration A (Payout)

**ASSUMPTIONS**

- Current Age: 50
- Initial Transfer: $100,000
- Retire Age/Status: 65 Single
- Biweekly Contribution: $100
- Market Condition: Up 7.56% (Accumulation) – Up 7.98% (Payout)
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<table>
<thead>
<tr>
<th>Lifetime Annual Withdrawal</th>
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<tbody>
<tr>
<td>Amt Initial: $16,530</td>
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<tr>
<td>At 75: $17,340</td>
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<tr>
<td>At 85: $18,170</td>
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<td>At 95: $19,520</td>
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<tr>
<td>At 75: $327,850</td>
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<tr>
<td>At 85: $346,190</td>
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<td>At 95: $306,070</td>
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IncomeFlex Illustration B (Accumulation)

**ASSUMPTIONS**

- Current Age: 50
- Initial Transfer: $100,000
- Retire Age/Status: 65 Single
- Biweekly Contribution: $100
- Market Condition: Flat 0% Return (Accumulation)
- Flat 0% Return (Payout)
- Guarantee Fee: 100bp
- Management Fee: 63bp

**Values at Lock-In age 65:**

- Highest Birthday Value: $139,000
- IncomeFlex Market Value/ 0% return: $113,000

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**IncomeFlex Illustration B (Payout)**

**ASSUMPTIONS**
- Current Age: 50
- Initial Transfer: $100,000
- Retire Age/Status: 65 Single
- Biweekly Contribution: $100
- Market Condition: Flat 0% Return (Accumulation) – Flat 0% Return (Payout)
- Guarantee Fee: 100bp
- Management Fee: 63bp

**Lifetime Annual Withdrawal**
- Amt Initial: $6,950
- At 75: $6,950
- At 85: $6,950
- At 95: $6,950

**IncomeFlex Market Value**
- At Lock-In: $113,000
- At 75: $28,300
- At 85: $0
- At 95: $0

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ASSUMPTIONS

| Current Age:  | 50  | Initial Transfer: | $100,000 |
| Retire Age:   | 65  | Biweekly Contribution: | $100   |

Market Condition: Flat Down 50% year before lock in (Accumulation) – Flat (Payout)

Guarantee Fee: 100bp  Management Fee: 63bp

Values at Lock-In age 65

- Highest Birthday Value: $139,000
- IncomeFlex Market Value: $53,515

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ASSUMPTIONS

Current Age: 50  Initial Transfer: $100,000
Retire Age: 65  Biweekly Contribution: $100
Market Condition: Flat Down 50% year before lock in (Accumulation) – Flat (Payout)

(Payout) Guarantee Fee: 100bp  Management Fee: 63bp

Lifetime Annual Withdrawal

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Guarantees are based on the claims-paying ability of the insurance company and are subject to certain limitations, terms and conditions. To maintain the IncomeFlex benefit, you must invest in one or more Prudential IncomeFlex Funds. Like all variable investments, these funds may lose value. Withdrawals in excess of the guaranteed lifetime income amount will reduce future guaranteed withdrawals proportionately.

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