



Longevity Insurance and Retirement Plans

Jason S. Scott

Managing Director, Retiree Research Center
Financial Engines, Inc.

May 13, 2010



Longevity Insurance Overview¹

- **What is Longevity Insurance?²**
 - Purchased at retirement (e.g. age 65)
 - Payouts begin in the **future** (e.g. age 85)
 - Similar to an immediate annuity without initial payouts
- **Advantages of Longevity Insurance**
 - Focus on high value insurance
 - Small allocation (10-15%) for large spending increase (20-30%)
 - Efficient way to get majority of annuity benefits

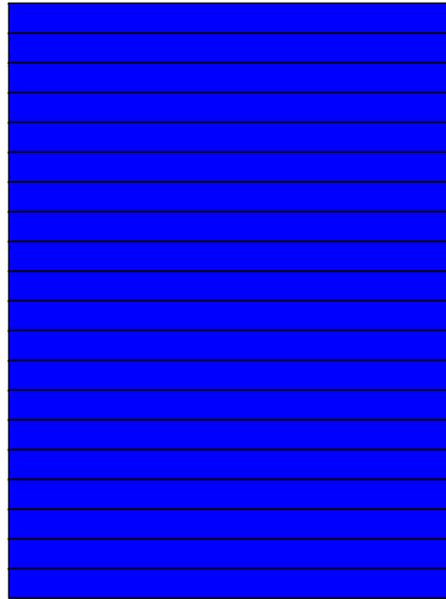
¹All rights reserved. Prepared exclusively for the EBRI Policy Forum #66. No further distribution rights granted without express written consent of author. Financial Engines® and we make it *personal*® are registered trademarks of Financial Engines, Inc. All views and opinions in this presentation are those of the author and do not necessarily reflect those of Financial Engines, Inc. Presented for discussion purposes only and is not indicative of any potential or actual product or service offerings. Not intended to solicit the sale, purchase, or offering of any securities, products, or service. Costs and hypotheticals presented for informational and evaluative purposes only.

²For discussion purposes only. Does not constitute offer to buy or sell an annuity product.

Insurance Costs Depend on Payout Chance



\$100



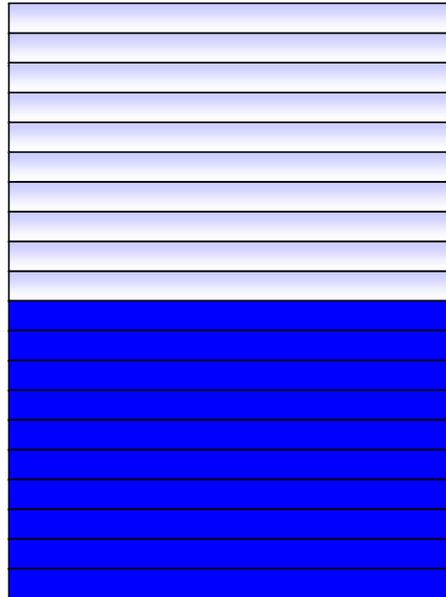
Insurance Payout (\$100)

X

Chance of Payout (5%)

Insurance Costs Depend on Payout Chance

\$50



Insurance Payout → \$100

X

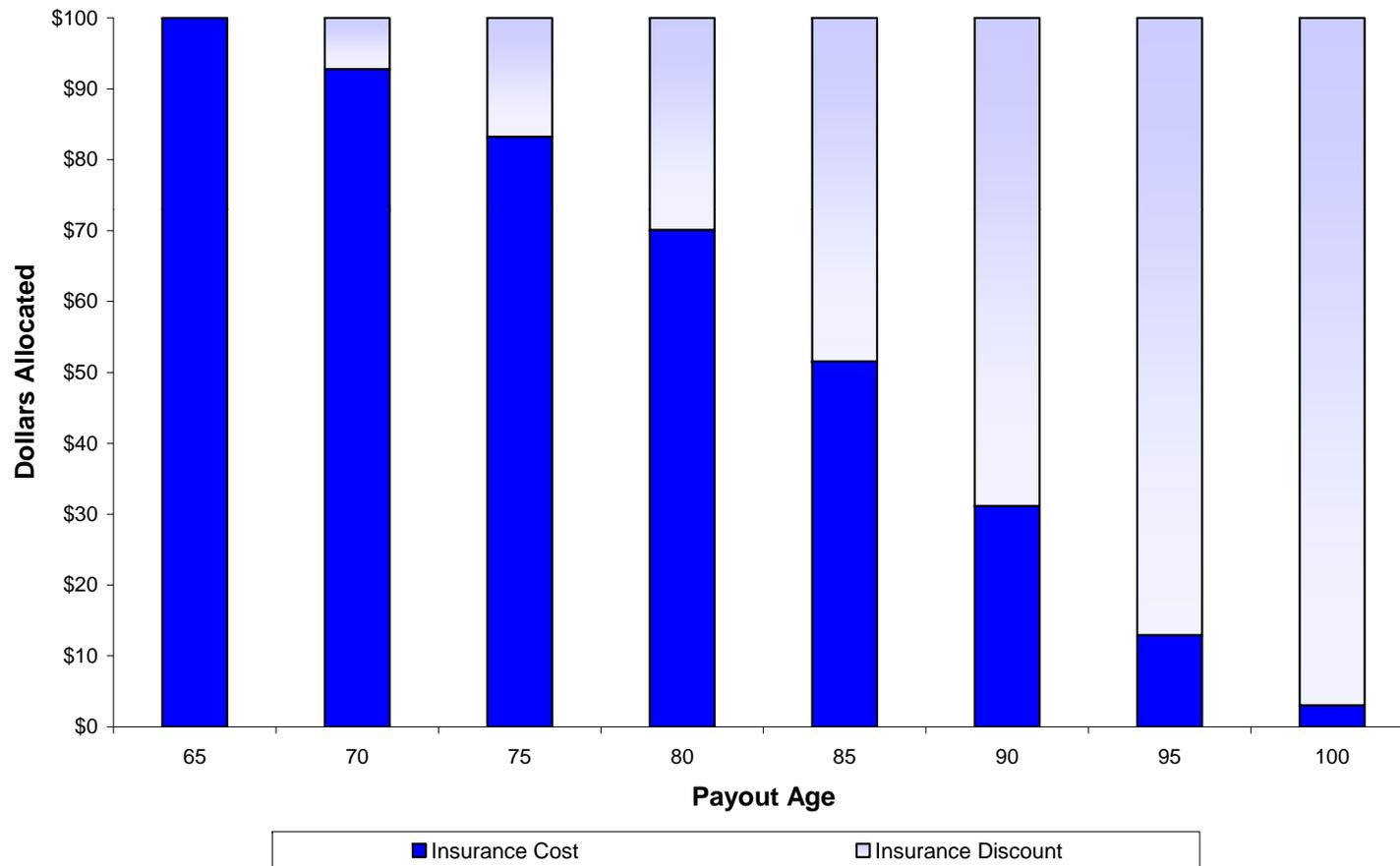
Chance of Payout → 50%

Insurance Cost → \$50

Annuity Income Decomposition

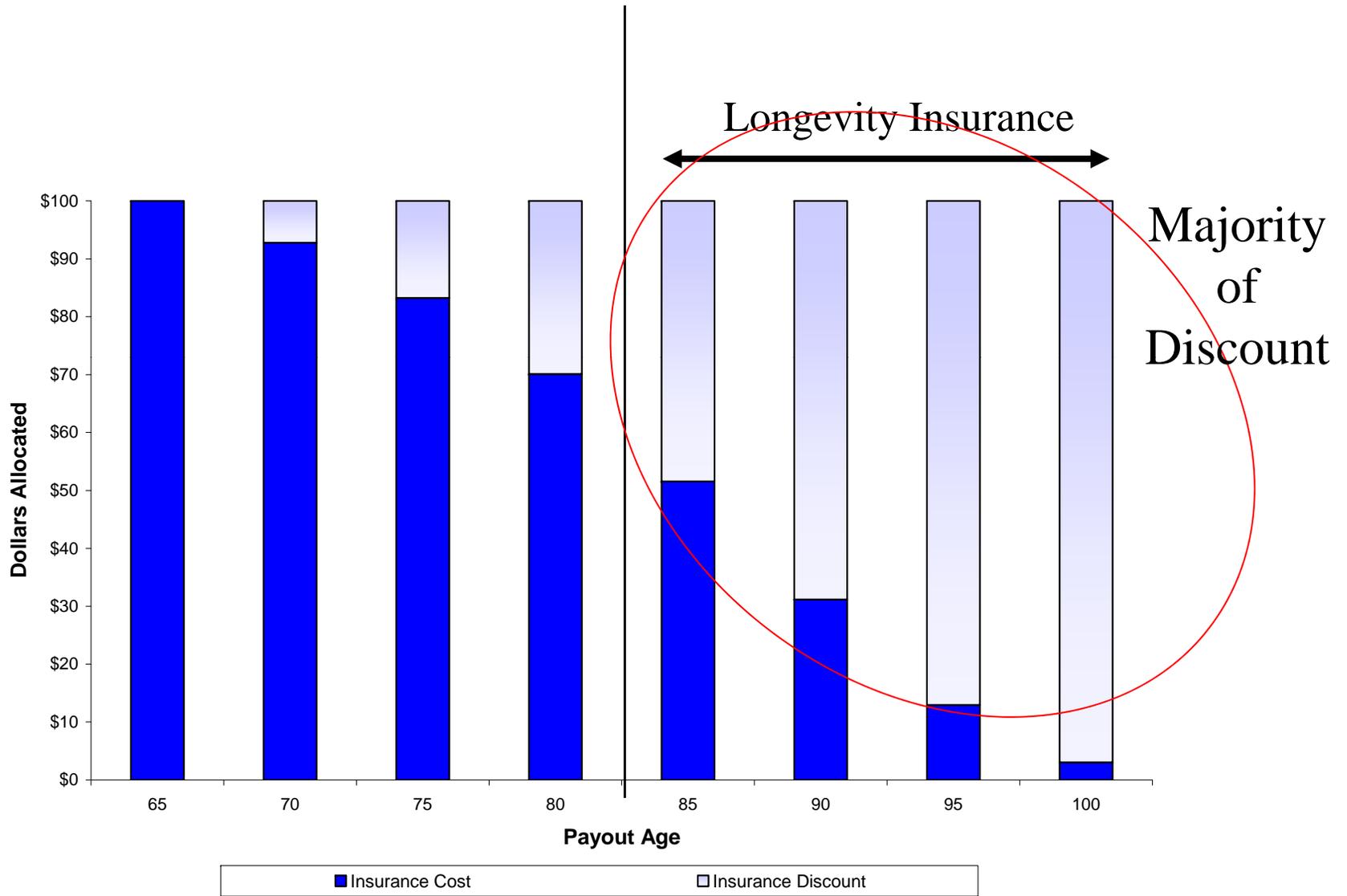
Cost Savings with Annuity Income

Age 65, Male



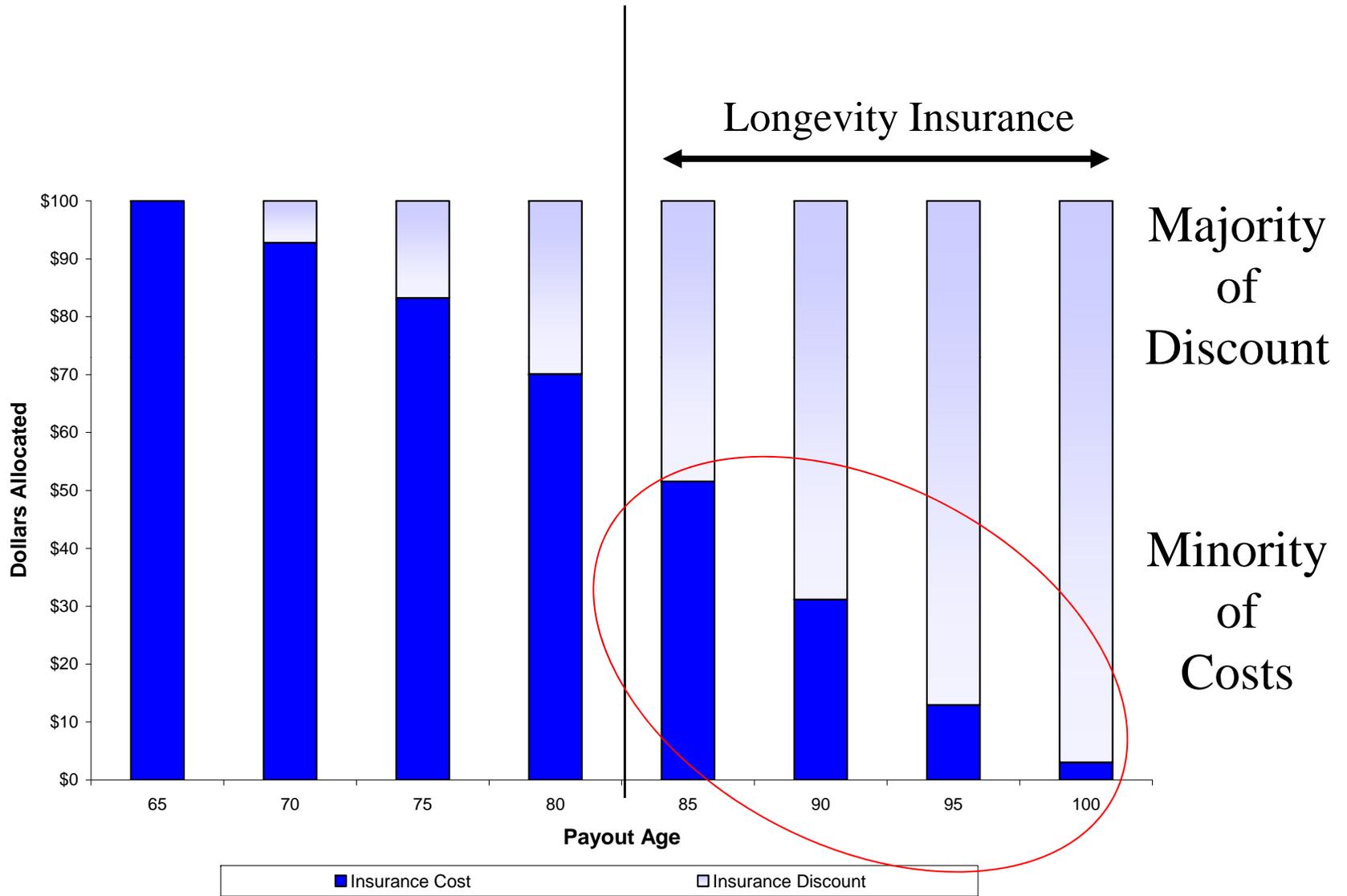
Costs and hypotheticals presented for informational and evaluative purposes only.

Longevity Insurance



Costs and hypotheticals presented for informational and evaluative purposes only.

Longevity Insurance



Costs and hypotheticals presented for informational and evaluative purposes only.

Insurance Illustrations¹

Income from \$1,000,000²
Male, Age 65

Annuity Type	Annuity Allocation	Spending (Increase)	Insurance Benefit (%)
None	0%	\$57,557 (n/a)	0%
Immediate	100%	\$80,923 (+\$23,366)	100%
Immediate	20%	\$62,230 (+4,673)	20%

¹For discussion purposes only. Does not constitute offer to buy or sell an annuity product. Annuity information, costs, and hypotheticals presented for theory discussion purposes only.

²Source – Scott, J.S. 2008. The Longevity Annuity: An Annuity for Everyone? *Financial Analysts Journal*. 64(1): 40-48

Insurance Illustrations¹

Income from \$1,000,000²
Male, Age 65

Annuity Type	Annuity Allocation	Spending (Increase)	Insurance Benefit (%)
None	0%	\$57,557 (n/a)	0%
Immediate	100%	\$80,923 (+\$23,366)	100%
Immediate	20%	\$62,230 (+\$4,673)	20%
Longevity (85)	8.2%	\$70,175 (+\$12,618)	54%

¹For discussion purposes only. Does not constitute offer to buy or sell an annuity product. Annuity information, costs, and hypotheticals presented for theory discussion purposes only.

²Source – Scott, J.S. 2008. The Longevity Annuity: An Annuity for Everyone? *Financial Analysts Journal*. 64(1): 40-48

Policy Implications – DC Plans



- **Voluntary annuitization**
 - 100% very unlikely
 - 10% possible → Longevity insurance much larger impact

- **Employer match**
 - DC plan covers funding from 65-85, employer covers late years?
 - Typical match levels sufficient for longevity insurance purchase

- **Required Minimum Distribution (RMD)**
 - Longevity insurance is non-compliant with RMD rules
 - Exemption (similar to immediate annuity) likely needed

Policy Implications – DB Plans

- **Lump sum distributions**
 - New option: 90% lump sum / 10% longevity insurance
 - Retains majority of insurance benefits

- **Discontinued DB Plans**
 - Replace DB → DC with DB → DC + Longevity insurance
 - Dramatically lowers DB support costs (90%)
 - Retains majority of insurance benefit

- **Summary**
 - Individuals seem to like liquidity
 - Longevity insurance -- low cost + high benefit
 - Current DB/DC plans enhanced with longevity insurance could allow individuals to have both liquid assets and insurance benefits