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Considering target date funds with lifetime income benefits

As the interest and desire to offer a lifetime income solution within retirement plan lineups continue to grow, plan sponsors and advisors are looking for guidance on how to begin the evaluation process. Including a lifetime income solution within a familiar structure of a target date fund (TDF) can offer participants the benefits of an annuity in a cost-efficient and easier-to-manage product, while providing them with a level of comfort and confidence as they approach retirement.

Not all target date funds are built the same. At Nuveen, we believe in-plan target date funds should be built, first, to improve expected accumulation outcomes. Why? The results should yield larger, and/or more risk-controlled nest eggs that will sustain a lifetime in retirement. This feature benefits every participant invested in the target date fund. Next, the solution should address decumulation. Participants should have the option but not necessarily the obligation to annuitize at retirement. Finally, the solutions should be affordable.

Why a target date fund with lifetime income?

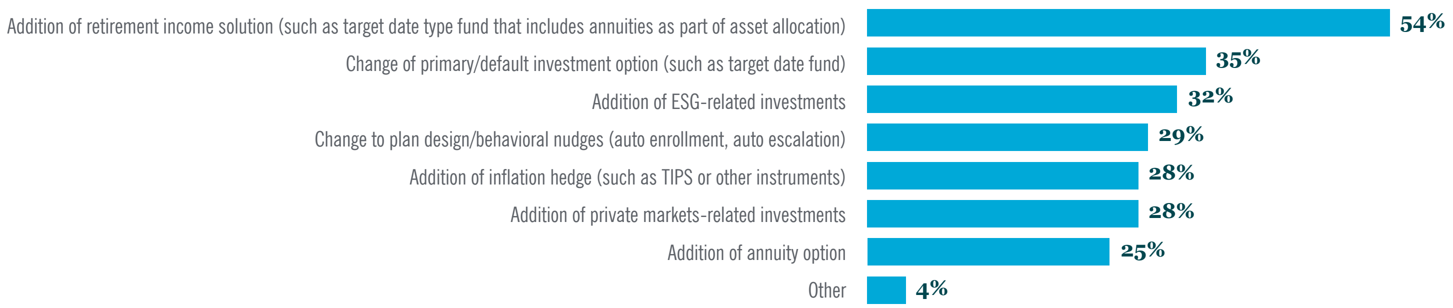
There is demand among plan participants for guaranteed retirement income. According to AARP, half of Americans said they worry most about running out of money in retirement, while more than two-thirds of U.S. workers said they would choose an employer if it offered a lifetime income benefit. Participants understand that guaranteed income can play a significant role in securing their retirement.

Plan sponsors recognize that a guaranteed income solution can improve participants' risk/return profile to better prepare them for retirement. In fact, in a recent Nuveen survey, sponsors stated that adding a lifetime income option to their plan lineup is at the top of their lists of recent or upcoming changes.

49% Americans who say running out of money is their biggest retirement concern[1]

70% Workers would choose to work for, or stay with, a company that offers access to guaranteed lifetime income in retirement[2]

WHICH OF THE FOLLOWING CHANGES DID YOU MAKE OR PLAN TO MAKE? (N = 69)



Overall (n = 69 respondents making changes to their DC investment menu in the coming 2 years). % Yes, multiple answers allowed.

How a TDF integrates lifetime income

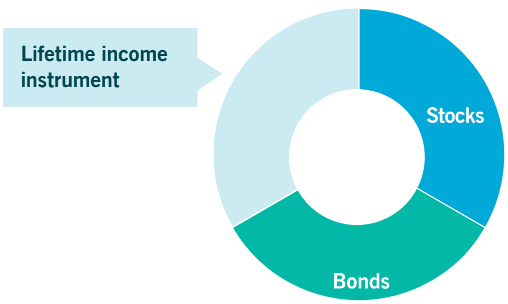
As sponsors seek to integrate lifetime income into their TDF allocations, they typically choose from two approaches.

1 Allocation to a lifetime income instrument, alongside stocks and bonds

The allocation to a lifetime income instrument (annuity) is backed by an insurance account (e.g., a "General" or a "Separate" Account). As an allocation within the target date fund, the annuity receives contributions and will deliver a stream of guaranteed lifetime income upon annuitization.

Importantly, differences in investment characteristics among lifetime income instruments will vary by provider. For example, some instruments are principal protected and deliver guaranteed returns with near zero volatility, while others introduce significant interest rate risk near, and during, retirement.

Target date fund allocates to lifetime income instrument

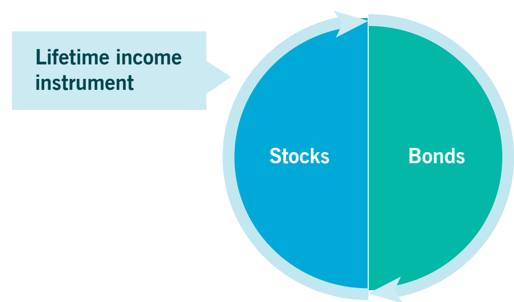


2 Wrap the target date fund with a lifetime income instrument

A Guaranteed Minimum Withdrawal Benefit ("GMWB") is an insurance contract (annuity) that wraps around the entire target date fund and guarantees a specified perpetual withdrawal percentage from the participant's accumulated benefit base.

The benefit base is the value upon which a GMWB makes the income payments, and it is generally a function of participant contributions and market activity. For example, if a participant's benefit base is $200k, and the GMWB benefit is 5%, then their annual income benefit is $10k.

Target date fund is wrapped with lifetime income instrument



How to evaluate and select a TDF with lifetime income

Choosing the right TDF with lifetime income can be complicated. We believe **three guiding principles** can help plan sponsors navigate the evolving landscape of target date solutions.

1 Change as little as possible.

Target date solutions work very well as currently constructed.

2 Design solutions for the broadest population of plan participants.

As a Qualified Default Investment Alternative (QDIA), the target date solution should be appropriate for all plan participants—even those who do not want to elect income.

3 Make the income benefit available to every plan participant.

Access should not be contingent on participants' age or contribution history.

As the retirement plan fiduciary begins the TDF evaluation, here are some key considerations when building a due diligence process. While this is not an exhaustive list, it's a good place to start. Understand that target date fund products differ in meaningful ways, so be sure to thoroughly document the decision making process.

PRODUCT CONSIDERATIONS

- ☐ **How is the income benefit being delivered, and is it guaranteed for life?**

  Lifetime income solutions range from preserving liquidity to mitigating longevity risk and come with various strategies and tradeoffs.

- ☐ **Are participants age-gated and restricted to investing in their age-appropriate TDF vintage, or can they freely invest in any TDF vintage?**

  Understand who enforces the age-gates, and what are the purpose of the age-gates.

- ☐ **Is the income benefit available to all plan participants, irrespective of their age and/or contribution history?**

  If the income benefit is only available to a subset of the participant population, be sure to document that.

- ☐ **Are there direct, or indirect, limits on the amount of income a participant can receive?**

  If a GMWB is being utilized, is there a cap on the benefit and is it periodically high watermarked?

- ☐ **Does the participant have flexibility when it comes to electing lifetime income?**

  Note if is it an option or obligation to elect lifetime income.

- ☐ **Is there a specific income election window?**

  Must the participant elect the income benefit within a specific timeframe? Or does the benefit automatically begin at a certain date/age?

- ☐ **What are the benefits of having exposure to the lifetime income component during the accumulation phase?**

  Does the lifetime income component have a guaranteed minimum crediting rate? Is the exposure protected from losing value?

- ☐ **Can the lifetime income payments increase in retirement?**

  Are there cost-of-living adjustments or other forms of increases in retirement?

- ☐ **Are the TDF fees competitive?**

  If there is an additional cost to include lifetime income, understand how the additional layer of fees might impact savings and income in retirement.

- ☐ **Is the TDF and the income benefit portable?**

  Plan-level portable? Participant-level portable?

LIFETIME INCOME LINGO*

- A **Deferred Fixed Annuity (DFA)** provides guaranteed returns — dampening total portfolio volatility — during accumulation, and pays guaranteed lifetime income during retirement.
- A **Qualified Longevity Annuity Contract (QLAC)** provides income payments at a postponed future date, typically beginning after the participant has turned 80 years old.
- A **Guaranteed Minimum Withdrawal Benefit (GMWB)** guarantees a specified perpetual withdrawal % from the participant's accumulated benefit base.

QUICK TIP:

Consider, and document, the pros and cons of TDFs that give participants the option to elect income vs. those that require participants to elect income. For those TDFs that allocate to an underlying annuity solution, be sure to document how the annuity allocation impacts the investment characteristics of the total TDF portfolio. For example, does it provide investment benefits for those participants who do not plan on electing income?

Given the demand for lifetime income, there is opportunity for plan sponsors to provide a more secure retirement for employees. Guaranteed income solutions packaged in a target date fund can be a relatively simple and cost-efficient way to do so. For sponsors that choose this option, following a few principles and answering some key questions will prepare them to successfully integrate lifetime income benefits into a TDF.

*Visit **nuveen.com/lifetimeincome** to learn more about the benefits of protected savings and guaranteed lifetime income.*

Endnotes

1 AARP, May 2019.

2 TIAA 2021 Lifetime Income Survey, May 2021.

* **All guarantees are based on the claims-paying abilities of the issuing companies.**

The target date is the approximate date when investors plan to start withdrawing their money. The principal value of a CIT is not guaranteed at any time, including at the target date. After 30 years past when the target-date has been reached, a CIT may be merged into another target-date CIT with the same asset allocation. The unit value of a CIT will fluctuate, and investors may lose money. A CIT may not achieve its target allocations and even if it does, the asset allocations may not achieve the desired risk-return characteristics and may result in the CIT underperforming other similar funds.