AllianceBernstein’s Multi-Insurer In-Plan Annuity

By Kerry Pechter *Wed, Dec 1, 2010*

To make sure that the glide paths of plan participants' TDFs lead to a 'safe landing,' asset manager AllianceBernstein has enlisted three insurers--AXA Equitable, Lincoln and Nationwide--to equip them with stand-alone living benefits.

Investment management giant AllianceBernstein has formed an alliance with three of the largest annuity issuers—AXA Equitable, Lincoln Financial, and Nationwide—to offer defined contribution plan participants a way to turn their target date funds into a lifetime income stream.

Under the new program, which the company calls Secure Retirement Strategies, plan participants who invest in AllianceBernstein’s target date funds will, about 20 years before retirement, begin protecting that money with a so-called stand-alone living benefit that provides an income that the participant can’t outlive.

Attaching stand-alone lifetime income benefits to target date funds in 401(k) plans isn’t new—Prudential Retirement has been doing it for several years through its IncomeFlex program and Great-West Life & Annuity’s retirement division began marketing a similar program to plan sponsors last spring.

What’s new is that three insurance companies are collaborating to provide the living benefit, not one. AllianceBernstein will face the client, and it has created a proprietary administration system called GATES (Guarantee Aggregation, Trading and Expensing System) to handle the job. But behind the scenes, AXA Equitable, Lincoln and Nationwide will be splitting the task of providing the living benefit.

On a tactical level, AllianceBernstein hopes that this three-legged approach, and the diversification it provides, will quell plan sponsors’ queasiness about liability in case their plan’s insurer defaults on its obligations down the road. For some sponsors, it probably will. Others won’t feel safe offering annuities until the Department of Labor offers an explicit “safe harbor” that exempts them from future risk.

On a strategic level, the $496 billion (as of 12/31/2009) manager of defined benefit, DC and individual assets, wants to find ways to retain participant money under management more or less permanently. Indeed, all of the big institutional investment managers are maneuvering to hold onto the Boomer assets they have and add as much to them as possible. It’s a 21st century financial version of the Great Game, where the prize is management fees on a pool of trillions in savings as rather than Central Asian oil and gas.

How SRS works

Secure Retirement Strategies works like existing SALB programs. When plan participants who have invested in Alliance Bernstein target date funds (whose other managers are bond specialist PIMCO, large-cap value equity specialist Wellington Management and index specialist State Street Global Advisors) reach their mid to late 40s, they begin purchasing a rider that puts a floor under the “benefit base”—the notional amount on which future income payments will be based.

As participants make their period contributions to their TDFs, AXA Equitable Life (whose parent, AXA Financial, owns 63% of AllianceBernstein), Nationwide, and Lincoln Financial, will compete to guarantee a future chunk of income based on each contribution. The guaranteed payout rates fluctuate with market conditions. They’re also based on the age of participant at the time he or she makes the contribution. That is, earlier contributions buy more future income than later contributions. The standard fee for the guarantee is one percent, although plan sponsors can buy a richer guarantee by paying more.

“It sounds complicated but the components are all available today,” said Mark N. Fortier, CFA, head of the SRS project at AllianceBernstein. “A TDF does virtually the same thing with multiple investment managers.” [See accompanying feature, “The Point Person for Secure Retirement Strategies.”]

Nationwide became involved in the project after receiving a request for proposal from AllianceBernstein in 2009. “They were looking for multiple insurers [for their project] and we were interested in trying to penetrate the in-plan guarantee market,” said Cathy Marasco, assistant vice president, Nationwide’s Individual Investments Group. AllianceBernstein sought proposals from eight or nine strong insurers at the beginning of the project, Fortier told RIJ. All three of the finalists have A+ ratings (second of 16 categories) from A.M. Best.

AllianceBernstein provides investment options for Nationwide’s retirement plans, but the companies don’t compete directly in the institutional arena. AllianceBernstein focuses on larger plans and Nationwide focuses on large plans only in the public pension market. The deal gives AXA Equitable and Lincoln access to a large plan market they don’t ordinarily reach, Fortier said. Lincoln was not available for comment and AXA referred all questions to AllianceBernstein.

“We’re just providing the guarantee behind the scenes,” Marasco said. “The participants think they have one guarantee but actually their guarantee is split across three insurers. We’ve looked at other designs where there was a lead insurer and a reinsurer. But in this case we own our guarantee and we’re not taking on the risk of the other insurers.

“Each insurer will set its own guaranteed income rates quarterly,” she added. “[Regarding fees], we agreed upon a price, but we have the flexibility to change the payout rate based on the market environment and hedging costs.”

Outside perspectives

Prudential, whose IncomeFlex program pioneered the addition of stand-alone living benefits to target date funds, is watching the AllianceBernstein effort. The Newark, N.J. based company, the leading seller of individual variable annuity contracts, thinks the three insurer approach solves some problems but creates others.

“We emerged from the financial crisis stronger than ever and we’re leveraging that advantage. So we haven’t had to go the multi insurer solution,” said Brent Walder, senior vice president in Institutional Income Innovations, Prudential Retirement. “We have over 1,000 plans, and our plan sponsors are comfortable with a single insurer solution. We’ve had a lot of dialogues with very large plan sponsors [about liability].

"One way to solve that need is the AllianceBernstein way and split it three ways. You have a higher likelihood of a problem but less severity if one happens. But as you introduce more insurers, there's more to explain. You have different withdrawal rates for different contributions. Our product is more straightforward and simpler. Those are the tradeoffs."

Also watching the AllianceBernstein launch is Ron Surz, president of Target Date Solutions in San Clemente, Calif., who designs custom target date funds and is an advocate of TDFs that have zero equity allocation at the planned retirement date. (AllianceBernstein's institutional TDFs reach a 50% equity allocation at maturity and maintain it through retirement. That makes them easier to hedge than than the firm's retail TDFs, which have up to a 60% equity allocation at the retirement date.)

Surz thinks that SRS is a step-forward but not a complete retirement income solution for plan participants. "The desire to 'DB-ize' DC plans is reasonable and honorable on its surface, but [the retirement income challenge] requires something more creative than jamming retirees into anything, like annuities and/or GLWBs," Surz told RIJ. "Retirement is way too complex for a one-size-fits-all solution. So the majority should opt out. Those who don't opt out might be better off with a GLWB than not, but they would be best served by some serious education and review of their options.

"As Einstein said, 'We cannot solve today's problems at the same level of thinking that created them,'" Surz added. "I personally don't believe that the 'solution' is currently sitting on a GLWB shelf. But I applaud the efforts to seek out a better way. I also believe that we still haven't properly tackled the much simpler accumulation phase, where product is primarily designed for profit rather than for the benefit of the participant."

Liability concerns

Skepticism persists regarding the willingness of plan sponsors to accept in-plan annuities if they can be held responsible for the failure of the insurance partner they choose. "Having the opportunity to diversify the provider risk is something sponsors are interested in," one observer close to the situation said. "But with this the participant is still getting a sponsor-selected solution.

"You have to remember that the plan sponsors' confidence in the financial services industry has been shaken deeply. Until they feel that there's a clear way to deal with the fiduciary liability, they won't get excited about this. Some will pick it up but not others," he added.

But he thought that AllianceBernstein was well-qualified be an innovator in the in-plan annuity area. "They *get* the plan sponsors more than a lot of other groups—maybe because they're such a great plan sponsor themselves. They work hard at their own program. There's no 'shoemaker's children' there," he said.

Lew Minsky, the executive director of the recently-formed Defined Contribution Institutional Investment Association, which is composed of large asset managers, including AllianceBernstein, has also been following the SRS launch closely.

“We went to five cities and talked to large plan sponsors and the most common concern was single insurer risk,” he told RIJ. “Whether it’s a real or a perceived issue, its been holding plan sponsors back from moving forward. That’s one of the things that AllianceBernstein saw in the marketplace. And they saw that if they could get plan sponsors past that issue it would be very impactful.

“AllianceBernstein has been working on this for a couple of years. It’s an incredibly complex and difficult process to get insurers together to collaborate. You’ve got competing companies with their own business interests and historical differences. There are no anti-trust issues here, as far as I know, but you have a group of companies working in their individual business interests.

“In this case, they’ve decided that it’s in their business interest and in the broader interests of the industry to move this product forward. Equally important, from an industry evolution perspective, [is that] a certain group of insurers sees an unrealized opportunity in the in-plan market, but they’ve had real challenges in taking advantage of it. They see this as a way to tap into that opportunity.

“But I think asset managers in general, and AllianceBernstein in particular, as part of serving the DC marketplace, are honestly trying to figure out the best way to design to design these long-term default investment structures,” Minsky added. “That involves planning for accumulation and decumulation.

“I expect to see other companies trying this. I know of a couple of large sponsors that are looking at doing similar things with their custom target date funds, and one employer that’s looking at forming a multiple insurer pool. We have to get people away from a simple focus on accumulation, and this definitely speaks to that.”