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'Income America' Offers '5ForLife'

By Kerry Pechter *Thu, Mar 4, 2021*

'Our clients are so past proprietary solutions," said Scott Colangelo, who brought Lincoln Financial, Nationwide, American Century funds, Vanguard, Fidelity and others together to create Income America 5ForLife, an in-plan 401(k) annuity. 'This won't be anybody's single product,' he said. 'No one has ever done that before." (Photo from Income America brochure.)

The idea for Income America 5ForLife, the latest in a wave of new methods to add lifetime income options to 401(k) plans, was born on a flight from Houston to Kansas City in late October 2014.

Scott Colangelo, the founder of Qualified Plan Advisors, and his ERISA attorney, Matthew Eickman, were parsing an internal letter from a Labor Department official to a Treasury official. The DOL had given its blessing to auto-enrollment of plan participants into target date funds with annuities tucked inside.

For Colangelo, whose companies serve as fiduciaries and advisers to some 700 retirement plans, and that letter was a green light to the future. Yesterday, he unveiled his concept for making defined contribution more pension-like was unveiled to the world.

He came up with the name, "**Income America.**" If that sounds too much like a Marvel Comics team of heroes, especially for a new venture in an unproven market, consider Colangelo's collaborators:

Prime Capital Investment Advisors (Colangelo's registered investment adviser or RIA); Lincoln Financial and Nationwide (as co-guarantors of the 5ForLife group annuity); American Century (as TDF glide-path designer); Vanguard, Fidelity and Prudential (as fund providers); Wilmington Trust and Wilshire (as fiduciaries); and SS&C, whose "middleware" would wire it all together and ensure portability when participants change jobs.

In a nutshell: Income America is a series of target date funds with a novel type of guaranteed lifetime withdrawal benefit (GLWB) rider attached. The rider, called "5ForLife," promises to pay plan participants 5% of their benefit base (the greater of the account value or net contributions at age 65) every year for the rest of their life. It doesn't guarantee accumulation. The all-in expense ratio: 1.3% per year.

"We got some of the bigger competitors in the industry to come together, and 99% of it was positive," Colangelo told *RIJ* yesterday, in a party mood. "We're having 70 people on a virtual happy hour tonight."

Since last fall, several firms have brought new retirement plan solutions to the 401(k) market. They've responded to provisions in the Secure Act of 2019 (effective January 1, 2021) that, among other things, aimed to make plan sponsors less nervous about offering annuities to their participants.

These companies all believe that plan sponsors and participants want income solutions, and are willing to pay for them. That remains unproven. But the $5 trillion 401(k) market is much too big to ignore—especially when so much of those assets are escaping (irrevocably) into brokerage rollover IRAs.

'We're so past' proprietary solutions

In the years since Colangelo began developing Income America, Prudential, Great-West and others have tried yoking TDFs with lifetime withdrawal benefits, without notable success. We asked Colangelo why he thinks Income America can succeed where those pioneers didn't.

One reason, he said, is Income America's flexibility. Previous products tended to come from a single life insurer, single record keeper and single fund provider. When Income America is sold by Colangelo's advisers, they can offer the plan sponsor either a Lincoln or Nationwide guarantee, and act as fiduciaries or recordkeepers themselves. Lincoln Financial or Nationwide or American Century representatives can sell Income America, and offer their own recordkeeping services and services of other members of the consortium. A plan sponsor can choose to start the commencement date of the guarantee at age 45, 50 or 55, depending on what they think suits their participants.

Scott Colangelo

"Our clients are so past proprietary solutions," Colangelo told *RIJ*."This won't be anybody's single product. It will be a consortium product. No one has ever done that before."

The other appeal is expected to be the simplicity of the guarantee. When participants reach age 65, they can start taking their 5% each year. There are no ratchets to lock in a participant's account gains from one year to the next, and no incentives for the client to delay taking income.

Behind the scenes, of course, there's considerable financial engineering. "This is neither a general account product nor a separate account structure, nor are they fixed annuities," Eickman told *RIJ*. "The insurance companies provide a GLWB rider, assess an annualized fee, then buy hedging mechanisms (such as 20-year swaps and other vehicles) to allow them to insure the risk."

At first glance, Income America, with its two life insurers, looks comparable to the three-life-insurer GLWB system that United Technologies uses. Every month, three companies bid for rights to insure incoming participant contributions, and the high bidder gets the lion's share of that month's contributions.

Bids at United Technology would fluctuate from month to month, depending on interest rates. In Income America, there is no bidding process. Lincoln and Nationwide levy their fee on half of the account balances.

As for the danger of Income America carving market share out of Lincoln or Nationwide's existing 401(k) business, Eric Henderson, president of annuities at Nationwide, dismissed that concern.

Eric Henderson

"We have a number of efforts in in-plan space, but in this case we're working with several different partners on something unique," he told *RIJ*. "Each of our offerings work a little differently. Plan sponsors might prefer one design over another. We'll let the employers choose which makes the most sense for them.

"This is a situation where a rising tide lifts all boats," he added. "We welcome the competition. Increasing the number of providers who make this type of solution available will raise its visibility. Employers will see it regularly. As they see more of their peers offering it, they'll feel pressure to do the same."

'Cost is a major factor'

To embrace Income America, or any similar program, plan sponsors will have to be comfortable with cost. Income America charges 1.3% per year of the participant's account value. If the 5ForLife rider were applied when the participant was 50, he or she might pay the fee for decades.

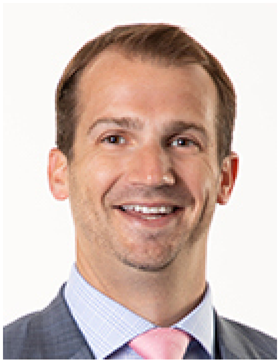
If they outlive their own money, the annuity issuers keeps paying them until they die. If they die before spending all their own money, their beneficiaries receive any remaining account value. Participants can drop the coverage any time, or take withdrawals from their account with no penalty. But, as with other GLWBs, withdrawals reduce the income stream.

"For plan sponsors, fees are their number one concern. Complexity and fiduciary risk is number two. The average passive fund costs in the single digits. You're asking a fiduciary to spend over 100 basis points [1%]," said Mark Fortier, one of the architects of the United Technologies plan.

Some look at the number of companies partnering on Income America and wonder how all of them can get paid. "I'm all for innovation, but cost is really a major factor." said Kelli Hueler, whose IncomeSolutions platform allows retirees to roll over their DC savings into a fixed immediate or deferred income annuity, in an environment where the annuity issuers competitively bid for their business. Her program requires participants to take the initiative, and the employers she works with seem to like that. "Plan sponsors tell us that they don't want to 'hard default' somebody into a benefit they may never take advantage of," Hueler told *RIJ*.

Today's low interest rates make it more expensive for annuity issuers to buy options to hedge their income guarantees, so Lincoln and Nationwide needed sharp pencils get the cost of a 5ForLife guarantee down to 0.975% within a total expense ratio of 1.3%. They did it by removing any promises to ratchet up the benefit base if the account value reached new high-water marks. The 45% equity allocation of the TDF during retirement presumably helps the support the guarantee as well, and the use of a CIT (collective investment trust) instead of a mutual fund as the product chassis helps keep costs and regulatory burdens low.

What happens if interest rates go up in the future? In that case, either the expense ratio of the product could go down or the payout at retirement could go up. Henderson said it was more likely that the cost could go down than that the payout would go up.



Matthew Eickman

Under US pension law, plan sponsors don't have to use the least expensive income solution. "The safe harbor provision [in the SECURE Act] doesn't say it has to be cheap. "It requires that the cost be reasonable in relation to the value provided by the solution's benefits and features, which inherently implicates an emphasis on value—not just low cost," said Matthew Eickman, the ERISA attorney and head of Prime Capital's retirement business.

"Strong, proactive fiduciaries start the inquiry from a different perspective. They ask, 'We know there will be cost; is [Income America] the best way to solve the income problem?' Informed fiduciaries certainly may justify a solution for the betterment of participants. In some plans, you can find good actively managed growth or foreign funds that alone cost 1.3%. The Income America solution provides much more value."

Given the potential for lawsuits over fees, plan sponsors are going to need help evaluating these income proposals, said Michelle Richter, founder of Fiduciary Insurance Services.

"This is yet another really creative solution entering the marketplace," she told *RIJ*. "Plan sponsors are not experts in annuities per se. So it's important that there are quantitative and qualitative services that help them analyze these new solutions quickly and clearly."

No one really knows yet if there's a market for income solutions in 401(k) plans. The federal government would like to see retirees keep their money in low-cost qualified plans, and not to run out of money. The annuity issuers and the fund companies who distribute funds primarily through 401(k) plans have arguably stronger incentives to pursue this business and make it work.

There are some $5 trillion in 401(k) plans, which makes them an irresistibly large target. But it's also a shrinking target. Retirees roll over hundreds of billions of dollars from 401(k) plans to individual brokerage IRAs every year. Annuity issuers and fund companies can make those assets much stickier by binding them into lifelong income contracts.

Eickman gave a piece of the credit for Income America to his friend Mark Iwry, who as deputy secretary of the US Treasury for retirement policy in 2014, was trying to tear down regulatory barriers to lifetime income products.

"It was all part of Mark's hope to stimulate interest and relax fiduciary fears. What Income America is doing is an indication that he succeeded in stimulating product development," said Eickman.

Iwry created the Qualified Longevity Annuity Contract, which removes an obstacle to buying a deferred income annuity with pre-tax savings. In 2014, *RIJ* and the Retirement Income Industry Association gave Iwry its annual Innovation Award for the effort.