United Technologies Adopts In-Plan Annuity

By Editor Test *Thu, Oct 6, 2011*

After overhauling its huge retirement plans, this Fortune 50 firm selected AllianceBernstein's stand-alone living benefit as its in-plan 401(k) income option. AXA Equitable, Nationwide, and Lincoln Financial were expected to support the lifetime guarantee.

The retirement industry has been waiting for a Fortune 100 company to set an example and be the first to add an in-plan income option to its 401(k) plan. Now one has.

United Technologies Corp., the Hartford, Conn.-based global conglomerate that builds Pratt & Whitney aircraft engines, Sikorsky helicopters and Otis elevators, has added what it described as an "unbundled" version of AllianceBernstein's Secure Retirement Strategies program to its $15 billion, 102,000-participant defined contribution plans.

Secure Retirement Strategies, which was described in a December 2010 RIJ article and accompanying feature, allows participants to invest in a series of target date funds, which can be covered by a "stand-alone living benefit" that works like the guaranteed lifetime withdrawal benefit of a variable annuity.

Three annuity issuers—AXA Equitable, Nationwide, and Lincoln Financial—will share responsibility for the guarantee, a spokesman for Nationwide told RIJ on Tuesday. (AXA Equitable and Lincoln Financial managers could not be reached for confirmation before deadline. UTC would not confirm the names of the participating insurers. UTC spokesperson Maureen Fitzgerald said that the insurer selection process was still ongoing.)

Mark Fortier of AllianceBernstein told RIJ Thursday that UTC, out of fiduciary concerns, will retain the flexibility to change insurers if they believe it is necessary, rather than accept them as part of an AllianceBernstein bundled product. "The ultimate decision regarding the insurers is theirs," he said. "If one of the insurers doesn't meet their criteria, they can change. That's the key distinction, as opposed to a packaged product where they don't have that choice. They need that safety valve."

UTC will be able to change insurers, for instance, if the insurer's price gets too high or if it runs into capacity problems—issues that are much more likely than outright insolvency. "Solvency is the last problem you'd have to deal with. Price competition and capacity come first," Fortier said.

The deal is significant on several levels, Fortier noted. It marks the first adoption of the in-plan lifetime withdrawal benefit by a major non-insurance corporation; it marks the introduction of personalized glide paths in target date funds; it gives each insurer the flexibility to adjust prices based on changing market and interest rate conditions; it gives a large company—one that has already fought ERISA class-action suits in court—the fiduciary protections that a large plan with huge potential exposures must have.

In the past, Fortier said, lack of adequate technology meant that target date fund issuers had to assign people to five-year buckets. When a stand-alone living benefit was added to a traditional TDF, it meant that people of different ages were treated as though they were the same age, thus inevitably discriminating against some. “To assume that everybody in a 2010 fund was 65 years old was flawed.” Today, he said, it’s technically possible to mass-customize TDFs and resolve that problem. “It’s the next logical evolution.”

Other companies offer in-plan options that attach a stand-alone living benefit to target date funds. Prudential was first-to-market with a solution called IncomeFlex. Diversified Investment Advisors, Transamerica and Vanguard collaborate on a program called SecurePath for Life, and Great-West Life offers a program called SecureFoundation. The UTC-AllianceBernstein deal, by setting a precedent for the establishment of an in-plan option at a jumbo plan, could create opportunities for all these providers.

Large corporations have a strong incentive to adopt in-plan income options in DC plans, Fortier noted. As large firms closed their DB plans and switched new employees to DC plans, they lost the ability to manage the workforce that DB plans have always provided. From their inception, DB plans have allowed companies to replace older employees with younger employees in a humane, predictable and orderly way. By adding an in-plan option to their DC plans, large companies can regain that capability.

UTC revised its two 401(k) plans for salaried and union employees in January, reducing the number of investment options and investment managers. It replaced actively managed equity funds with passive ones and cut fees. In March 2010, it changed record keepers, going to Aon Hewitt from Fidelity.

“As in other DC plans, investment options are arranged in tiers: a target-date fund series for people with the least experience in investing; a group of core funds for those with more investing experience; and a self-directed brokerage window of mutual funds for participants who say they are more active, savvy investors,” a May 30, 2011 P&I report said.

The lifetime income option provides an income solution for new employees, who are not eligible for UTC’s $17.6 billion defined benefit plan. It was closed to new employees at the end of 2009.

About two weeks ago, UTC announced that it would buy Goodrich Corp. for $16.5 billion, adding a maker of aircraft landing gear and jet-turbine casings to take advantage of a record surge in commercial plane orders.

In mid-September, ctpost.com reported that UTC unit Sikorsky Aircraft would cut three percent of its global workforce in the face of constrained commercial and military spending, or about 540 of the helicopter-maker’s 18,000 global workforce, of which 9,500 are based in Connecticut. In 2009, amid the financial crisis, UTC cut its global workforce of over 200,000 by more than 10,000 jobs.

Five years ago, UTC’s 401(k) plan was the one of the targets of unsuccessful lawsuits filed in four states accusing seven large companies of violating pension laws by allowing their employees to be overcharged by outside firms operating 401(k) retirement plans. UTC won all of the suits.

The employees were charged millions of dollars in excessive management fees, which often were hidden in obscure agreements and not disclosed to the workers, according to attorney Jerome Schlichter, who filed the suits in federal district courts in Connecticut, California, Illinois and Missouri.