Lifetime Income in 401(k) Plans: A Top-Down Consideration Framework

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Introduction

The focus on retirement income within employer-sponsored plans is an exciting step forward in the evolution of defined contribution plans. After years of halting progress, the time has come for these products to break into the 401(k) market in a meaningful way. Given improvements in product design, technology, and connectivity, retirement plan fiduciaries can envision the destination, but many are still looking for guidance on how to take the first steps to venture into this brave new world.

This paper outlines a top-down strategy to identify solutions that match high-level criteria based on plan sponsor preference. In some cases, solutions that seem similar based on overall design may suit very different preferences for plans. For example, when comparing solutions that use a fixed annuity within the glidepath of a target date portfolio that appears in an off-the-shelf design or a managed account, the basic concept is similar. However, the plan sponsor may already have plan design objectives one way or another.

The framework presented here is a practical representation of the choices available today that complements Broadridge's Prudent Practices for Retirement Income Solutions and assumes that plan fiduciaries take the steps outlined there. The Prudent Practices offer a validated process and valuable procedures, but they carefully (prudently, if you will) leave significant leeway to plan fiduciaries in how they implement evaluations.

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About the 401(k) Anuity Hub
The 401(k) Annuity Hub is an online subscription-based service for retirement plan fiduciaries to use when considering or evaluating lifetime income solutions. The approach is to provide essential facts and comparisons among products using a transparent and consistent framework.

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Background

The rise of the 401(k) has broadened worker access to defined contribution plans, and defaults have helped many participants save more in their retirement nest eggs. However, the process of converting those savings into sustainable retirement income remains an important shortcoming in many plans today. Decumulation isn't simply accumulation backwards since employees face an unknown lifespan and investment returns.

Workers may (too often, mistakenly) believe they can work an extra year or two if their plans for building retirement savings go awry. There's no equivalent once you're in retirement, especially as many people don't have the option of returning to work once they've handed in their last timesheet.

Increased retirement security is a potent workforce management tool that reduces anxiety about future retirement sustainability and enables workers to retire on time. Lifetime income is an inducement for hiring and retention and is especially attractive to the most productive and valuable workers.

Plan sponsors haven't been quick to add lifetime income to 401(k) plans despite the benefits to employers and participants. The path forward for plan fiduciaries hasn't been clear, given the diverse and growing array of new solutions in the marketplace. On top of this, the process of evaluating in-plan annuities is new territory for many.

Education and resources, including conceptual frameworks that simplify the process of identifying and selecting appropriate solutions, are key pieces of the puzzle to increase adoption of lifetime income.

Retirement Income and Lifetime Income

Retirement income broadly refers to both guaranteed and non-guaranteed income sources and strategies. Within the general category of retirement income, lifetime income includes annuities and solutions that incorporate an annuity in some way. This segment of products is uniquely valuable because it helps participants receive a reliable income similar to a pension that resembles the income they're accustomed to receiving from their employer paychecks.

The focus on lifetime income does not necessarily diminish the importance of non-guaranteed income during retirement; most people prefer a combination of a reliable retirement paycheck with withdrawals from non-guaranteed sources. However, the products and solutions are distinctly different from investment-based strategies and require knowledge that is new to many who are responsible for evaluating them.

In the time since the earliest workplace annuities came onto the scene, retirement itself has changed dramatically. Today, defaults, and in particular target date investments, are the products most employees rely on to provide retirement security. The advantage of target date investments is that they automate the complex task of managing retirement savings and investments, which is particularly valuable for those who are less financially knowledgeable or engaged.

Putting the "Retirement" in Retirement Plan

Philosophically, plan design should provide employees with a clear pathway to a secure retirement. The best way to provide this security is by reducing longevity risk through a lifetime income guarantee uniquely available through the use of an annuity. Offering annuities within a plan provides participants with easy access to lifetime income while retaining individual choice.

Bringing annuities into the equation means enlisting insurance companies, but target-date investments remain in the realm of asset management. Today, we see solutions that involve collaboration to varying degrees among insurance companies, asset managers, and product designers.

Naturally, these product providers are looking to marry the benefits of guaranteed lifetime income through an annuity with target date investments (including managed accounts). Many new lifetime income solutions emerging into the market recognize this trend, but there is no standardization in how they work, what kind of annuities they use, and even how those annuities generate lifetime income.

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These variations are necessary and offer choice to plan sponsors, but they may create some confusion—especially for those unfamiliar with annuities in the first place. And it's not much easier for someone who is already familiar with the individual annuity landscape, since the institutional products are quite different. Furthermore, the considerations for a retirement plan fiduciary are not the same as those of an individual when evaluating them for a plan serving the needs of a distinct participant population.

A Top-Down Approach for Plan Fiduciaries

The natural instinct with lifetime income is often to look first at the annuity design, but there are two fundamental flaws with this approach for plan fiduciaries. First and foremost, there are relatively few solutions actively marketed. Therefore, using the annuity as the starting point can limit the options for evaluation. Secondly, facts about the annuity in isolation do not provide enough information about how the solution fits into a plan. This is the case even when addressing structural choices and not diving into a fiduciary evaluation of specific offerings.

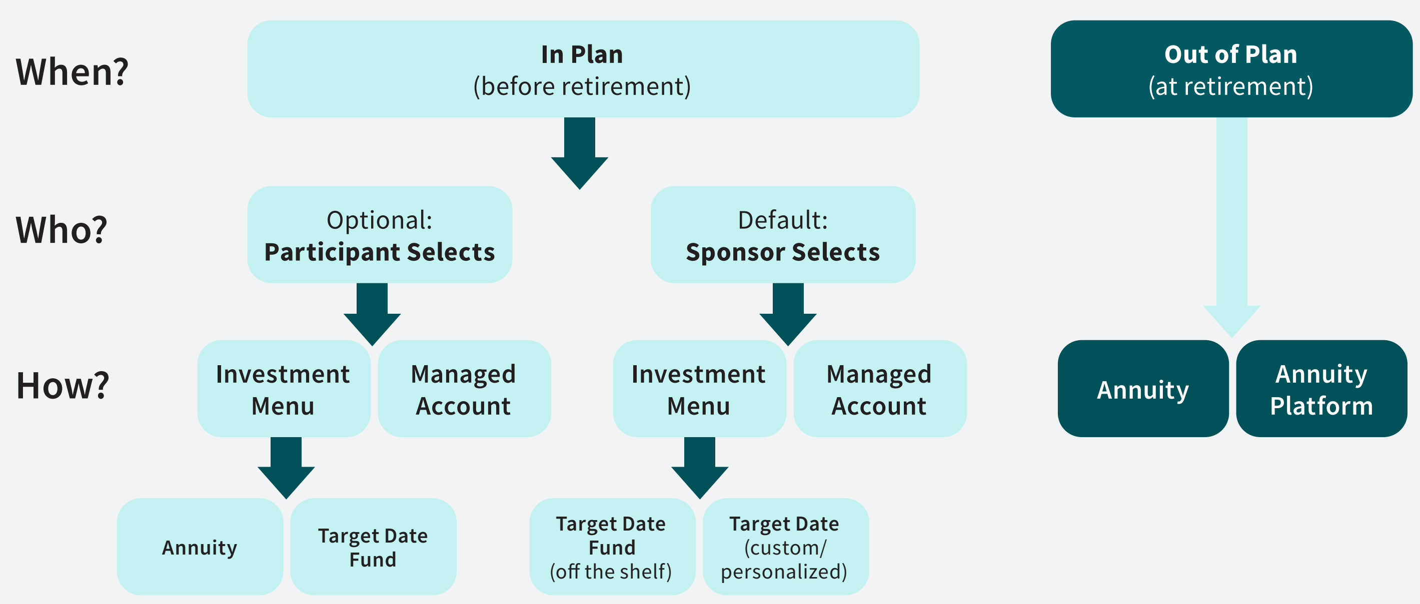
Therefore, using a top-down approach that considers fundamental questions about plan design allows a fiduciary to apply a basic filter to the available options and then conduct further analysis on a narrower set of choices. Evaluating a smaller selection of options that meet a plan's basic structural preferences and requirements makes it easier to identify the preferred choices and perform deeper due diligence to determine what, if any, solution is a good fit for the plan today.

Adding Lifetime Income

The decision to even consider adding lifetime income starts with the question of what the plan wants to accomplish. Is lifetime income a priority and, if so, what are the participant demographics and needs?

On one end of the spectrum, an employer may have an active defined benefit plan and therefore provide guaranteed income above and beyond what retirees will receive from Social Security. In these cases, it may be less important to incorporate annuities for all participants, yet even then some participants may want access to added income, whether that is because they have a lower pension benefit or a greater desire for income certainty.

Decision Tree for Retirement Plan Fiduciaries



Plan sponsors who have long-term employees and have closed a defined benefit pension plan may feel compelled to provide a defined contribution solution that provides lifetime income. Lifetime income can help employees confidently transition into retirement knowing they can supplement Social Security with lifetime income to meet essential expenses. Some employees may have little access to lifetime income; for example, teachers in some jurisdictions have a pension instead of Social Security, leaving them with a need for supplemental lifetime income.

There are important steps for implementation that include examination of the investment policy statement and whether the plan needs to make amendments.

The When, Who, and How of Lifetime Income Choice

As an initial step, you can break down the consideration of adding lifetime income to a plan into three questions:

When? Plan design can call for lifetime income solutions that are available to participants while they are still working (also referred to as "in plan") or that are available at retirement (also referred to as "out of plan").

Who? For a given solution, plan sponsors must determine whether they are most interested in a default target date investment that allows participants to decide if and when they receive lifetime income versus one that stands separately from default investments and requires each participant to actively make an election on their own.

How? Plan sponsors must decide how to deliver lifetime income solutions: as an investment option on the menu or through a traditional managed account solution. Target date investments (default or otherwise), when offered on the investment menu, may be pre-built or standard funds (off-the-shelf), be customized for the plan, or personalized for the participant. A traditional managed account offers options for managed portfolios and further tailoring.

A Word on Terminology

Internal consistency is more important than the establishment of definitive terms, but the broadest language is generally the most useful—and I've opted for terminology with a mind to simplicity and introducing the topic and ideas to more people. Many of the concepts discussed here can be described using different terms. And a single term may have different uses.

For example, "in plan" and "out of plan" effectively have three definitions (at least!). In practice, they all have their place and it's helpful to be aware of the nuance.

The advisor vernacular: Investments that are available during accumulation are "in plan" and those that are available at retirement are "out of plan."

A common recordkeeper perspective: Assets the recordkeeper administers are "in plan" and those that have left, by whatever means, are "out of plan." This view is agnostic to the process of annuitization; assets annuitized directly or rolled out are both no longer inside the plan.

The most technical: an annuity that is issued directly from retirement plan assets is "in plan" and one that is issued from an IRA is "out of plan." This may not seem like a significant distinction, but annuities offered under ERISA must be priced as gender neutral. Furthermore, the election of the annuity often requires notarized spousal consent and the plan sponsor is responsible as a fiduciary for the selection of issuing insurers.

On the other hand, it's possible to roll money out of the plan into an IRA, where the plan sponsor is no longer acting as a fiduciary. Some question whether the plan sponsor still bears some responsibility in this case, but there's no doubt that it's much less than with an annuity issued "in plan." Coming from an IRA, the spousal consent may not be required and it's possible to use gender-distinct pricing.

This nuance also causes misunderstandings with products that are considered "in plan" using the advisor vernacular but issue the annuity "out of plan," when a target date fund or annuity rolls into an IRA before income begins.

When?

In Plan: Before Retirement

Although the greatest value from an annuity is clear once people receive guaranteed income, they also can provide valuable protections in the period leading up to retirement. Aside from explicit guarantees of future income, they can insulate savers from market volatility. This is true whether an annuity is on its own or is part of a target date investment.

The income guarantee can wrap an entire equity-bond portfolio that constitutes all or part of the participant's plan assets. Fixed annuities offer returns that fit within the fixed income category but without the volatility that comes with bond funds, potentially replacing some of the bond allocation of a target date portfolio.

Furthermore, many participants seek the assurance of a pension-like income guarantee at retirement. That means that lifetime income that accumulates during the working years can be a valuable benefit that sets an employer apart—at least until workers start expecting it. This is true for both fixed and variable annuities.

Out of Plan: At Retirement

Lifetime income available at retirement gives participants the option to replace their paychecks with guaranteed income at the time when they are keenly focused on that concern. The ability to purchase a very straightforward single premium immediate annuity (SPIA) or other income annuity is the simplest path to offering lifetime income to participants.

Most importantly, the decision to add lifetime income in or out of plan is not an either-or, though the plan should evaluate each separately on its own merits. There is a strong rationale for offering annuities both before and at retirement. This may be the long-term strategy, even in situations where the plan sponsor opts to start with one or the other.

Sponsors can work directly with the insurer to make SPIAs or other income annuities available at retirement or they can use an annuity platform that may enable more choices and a more comprehensive participant experience.

Who?

A key plan design question is whether the sponsor establishes a default that includes the potential for lifetime income or the participant chooses it themselves off a menu.

For the sponsor, putting the decision fully in the hands of the participant offers access to a solution, but experience tells us that few participants elect the annuity. Defaults that include an annuity increase awareness of lifetime income and ensure that even those who pay little attention to the details of their plans will have the opportunity to learn about the option and make a decision later. Participants also see defaults as an endorsement by the plan sponsor, which increases their willingness to accept an allocation to an annuity at retirement.

Furthermore, "default" lifetime income does not imply that the participant automatically receives lifetime income by default at retirement; even when incorporated into a default, the participant always has control over whether to receive lifetime income in retirement.

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There is a longstanding argument that retirement planning itself is highly individual and poorly suited to cookie cutter models. As this is particularly true for the preference for lifetime income, the thinking goes, annuities have no place in a default solution.

The counterargument is that customization can take place at retirement, if it isn't already part of a more tailored approach in the run-up to retirement. Fully or partially automated personalization for participants is becoming increasingly available and technology can bring down those costs.

Naturally, it should be up to participants to drive the ultimate election of lifetime income, particularly when it comes to irrevocable payouts from income annuities (annuitization). Yet leaving this entirely up to participants who are unfamiliar with the value that lifetime income can provide without some form of accessible education leaves them very much in the dark.

After all, most people are unfamiliar with annuities and are not likely to select one from the investment menu or the list of distribution options at retirement. In the retail world, individual annuities are famously "sold, not bought," but they are also intended to fit a given planning need.

However, the approach to offering annuities within retirement plans is different because it's primarily about access. The plan sponsor's aim with an in-plan annuity is to make a vetted solution widely available to workers—no matter whether the sponsor places a raincheck in the participant's hands by attaching it to the default or the participant picks the annuity off the shelf themselves.

Qualified Default Investment Alternatives (QDIA)

The popularity of target date funds suggests that defaults are the best means to provide the protection that annuities offer as participants approach retirement. The inclusion of annuity within a default helps insulate savers from market volatility and gives them greater control over the timing of retirement by providing them with peace of mind during their working years.

It turns out that many workers believe that target date funds already provide income protection, so it's arguable that adding lifetime income simply gives workers a benefit they already expect.

The plan sponsor's aim with an in-plan annuity is to make a vetted solution widely available to workers.

Many companies also view defaulted lifetime income as an important benefit for workforce management, as it better enables workers to retire with confidence at the expected retirement age rather than continuing to work simply out of fear of outliving their savings in retirement. Furthermore, the default provides protection and an easier path to guaranteed income for disengaged employees who have not paid much attention to their retirement plans.

Any annuity that is part of a default and relies on the QDIA safe harbor must otherwise meet the QDIA requirements, including liquidity and the ability to change to different plan investment options. Therefore, a default that allocates to income protection can align with plan design objectives and is otherwise similar to other default investments.

In short, a default into an annuity does not mean a default into income. All allow for participant choice related to guaranteed income if they meet the safe harbor; there is no default solution on the market that irrevocably forces lifetime income on the participant. Today, there is a strong market preference to preserve participant choice.

Participant selection

A plan can place the responsibility for allocating to the annuity in the hands of the participant by including it on the investment menu for active selection. This provides a high degree of control to the participant; however, few may use it without significant intervention and education.

The design of the online experience, participant education, and other programs or purchasing services that will affect participant uptake are valuable factors when considering income options that the participant is responsible for electing.

How?

Annuities can sit alongside other investments on the investment menu but they cannot be placed inside a mutual fund. They can sit inside a collective investment trust (CIT) and many of the solutions today rely on a CIT. However, more tailored approaches are increasingly available, both within a target date structure and traditional managed accounts.

Investment Option

On the investment menu, annuities can appear on their own or as part of a target date fund.

- **Standard TDF:** off-the-shelf, usually CIT
- **Custom/Personalized TDF:** packaged solutions that are either customized (to the plan) or personalized (to the participant) based on recordkeeper data and potentially additional participant information

Traditional Managed Accounts

Traditional managed accounts offer different degrees of advisor engagement:

- Recordkeeper-driven Managed Accounts
- Advisor Managed Accounts

Traditional managed accounts rely on an advisor to provide some degree of advice, though improvements in technology have reduced the fees of these services in some cases and there is sometimes convergence with custom or personalized target date funds. In these cases, the annuity can reside within a "retirement income sleeve" or it can be incorporated overall as part of the investment pathway, which is particularly relevant for fixed annuities.

- **Recordkeeper-driven Models:** the advisor serves as a 3(21) fiduciary and uses an established investment model and recommends specific investments within the model
- **Advisor Managed Accounts:** the advisor has full investment discretion as a 3(38) fiduciary and may create and promote a proprietary investment strategy in addition to the selection of the investments

Finding the What: Lifetime Income Products

The final step of product selection involves understanding the different types of annuities, how they fit into the larger framework of other investments or distribution options, and the participant experience. Surveys overwhelmingly demonstrate that participants find the concept of lifetime income appealing—they want it in their retirement plans and may not otherwise seek out advice on buying an annuity outside the plan.

Lifetime income has been a part of retirement plans since the beginning—pensions and income annuities are the traditional cornerstone of retirement benefits. However, we're now facing the consequences of a shift from pensions to defined contribution that's emphasized accumulation and not income. Employers now have an opportunity to return the focus of defined contribution plans to the ultimate goal of retirement income security. They can also take advantage of contemporary product development that offers a diversity of annuities that offer new choices in how they fit into a plan and how they deliver lifetime income.

Technology opens the door to scalable solutions, better connectivity, and the ability to educate participants to better understand their retirement choices, whether that is while they are saving or actively planning retirement.

For today's plan fiduciaries, there is a growing array of solutions available, but the complexities of integrating annuities into retirement plans mean that there may not be many options within a single product category. Therefore, the traditional emphasis on apples-to-apples comparison that exists among accumulation solutions is less helpful when making decisions about income solutions.

Instead, plan fiduciaries can begin their evaluation of solutions based on plan preferences, such as using managed accounts versus off-the-shelf funds. The solutions available today can be quite different, even when they share high-level similarities. The particulars of both how lifetime income fits into the plan and how participants receive it make for purely operational distinctions.

A more detailed treatment of the topic of product comparison belongs elsewhere, but an understanding of the two forms of lifetime income from an annuity is fundamental.

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Annuitization vs. GLWB

One of the basic decisions that plan sponsors will make is what form of lifetime income they want to adopt in the plan since there are two means: traditional annuitization and the guaranteed lifetime withdrawal benefit (GLWB).

Annuitization

Annuitization is similar to a defined benefit pension. A retiree receives income for life in exchange for access to the savings that funded the annuity. The primary benefit of annuitization is that the payout is typically higher and the individual (or couple) will receive the money regularly no matter what. The guarantee is simple and there are death benefit options that allow heirs to receive payment(s) if the retiree dies within a certain period of time.

Annuitization can take place either directly from the plan or after a rollover into an IRA. These two alternatives have different implications, but, the assets are no longer administered from inside the plan.

Despite improvements to retirement sustainability that annuitization gives many retirees, many people are understandably reluctant to exchange savings for future income. Plan sponsors should consider the education and guidance that are available to help participants understand whether annuitization is right for them. Plan sponsors should also consider the options participants have to manage drawdowns from savings that aren't annuitized.

GLWB

A guaranteed lifetime income benefit, or GLWB, is structured as a lifetime income guarantee from an annuity product that does not require an irrevocable purchase of lifetime income. Instead, the annuity maintains a cash value but will pay a lifetime income even if the cash value goes to zero. The guarantee uses a theoretical value that's often called a "benefit base" that may be the same as the account value, though it can also be higher, especially before withdrawals begin.

The guaranteed income starts as a withdrawal of a percentage of the benefit base. For example, a retiree with a $200,000 benefit base and a 5% GLWB can withdraw at least $10,000 each year for a lifetime. Withdrawals always reduce the contract value but, if they're within the allowed amount, won't reduce the benefit base. If the guarantee structure allows the benefit base to increase after the individual starts taking withdrawals, the guaranteed income level can rise during retirement.

The GLWB offers more flexibility than annuitization, including the ability to take more than the allowed withdrawal amount and access funds from the account. However, doing so will reduce or eliminate the income guarantee. Plan sponsors should consider the education and guidance that are available to help participants understand how the benefit works and whether it is right for them.

The assets may remain within the plan or they may roll out into an IRA. Sponsors may benefit from retaining assets within a plan while also retaining fiduciary oversight of retired participants.

Plan sponsors should also consider how much of participants' savings is included in a GLWB and what procedures will protect retirees from the possibility of unintentional reduction of the income guarantee.

LIFETIME INCOME	FACTS	OPTIONS
Annuitization	• Exchange savings for guaranteed lifetime income • Income payments are administered outside of the plan • Death benefit options allow heirs to receive payments • Plan document may or may not need to allow annuities as a distribution option depending on the solution	• Payments for one person or a couple • Payouts can begin immediately or in the future • Annuitization can happen as a distribution from the plan or after rollover into an IRA
GLWB	• Withdraw from savings for income and guarantee payments begin when the account depletes • Savings remain accessible, declining with withdrawals • Plan documents may not need to allow annuities as a distribution option	• May be used with fixed or variable annuities • Accessing liquidity reduces the guaranteed income • The income guarantee (withdrawal amount) may increase before or after retirement depending on the guarantee design • GLWB assets can remain within the plan or roll into an IRA

Conclusion

Plan sponsors have a unique opportunity to strengthen the income security of employees through the use of innovative new solutions that blend investments and annuities. Education is the crucial element to the expanded adoption of in-plan annuities and many plan fiduciaries will likely take smaller steps before they make big moves. After all, they are trying to solve problems thoughtfully, not put out a fire with a blanket.

With more attention on the space, advisors and sponsors increasingly understand that these lifetime income solutions have benefited from retail annuity developments but evolved to fit defined contribution plans. Product iteration and innovation will continue but there are options available now to effectively meet the needs of many plans.

The first step is to consider whether a plan should, structurally, add lifetime income. If so, what options does the current recordkeeper offer? The ability to dig deeper into the plan preferences is predicated on understanding the product landscape and implementation options in the first place.

Momentum is on the side of participants to get access to the lifetime income that so many of them want—and more. You can think of the annuity as an anchor within the retirement income plan; a guarantee so often serves as the foundation that works with other distribution options to help people meet their goals in retirement.

Additional Reading

Michael Finke and Tamiko Toland, "Using Defaults to Enhance Adoption of Lifetime Income in Defined Contribution Plans," International Review of Financial Consumers, Volume 9 (2024): Issue 2 (December 2024), click for PDF at 401KAnnuityHub.com

Michael Finke and Tamiko Toland, "A Modest Proposal to Promote Retirement Income in 401(k)s," Journal of Pension Benefits, Volume 32, No. 3 (Spring 2025), click for PDF at 401KAnnuityHub.com

Tamiko Toland, "A Perspective on Evaluating Annuities for In-Plan Solutions," Journal of Pension Benefits, Volume 29, No. 1 (Autumn 2021), click for PDF at 401KAnnuityHub.com

Tamiko Toland, "The Fallacy of Institutional Pricing of Annuities," Journal of Pension Benefits, Volume 29, No. 4 (Summer 2022), click for PDF at 401KAnnuityHub.com

Tamiko Toland and Bonnie Treichel, "A Sticky Widget: Aligning ERISA Fiduciary Standards with Annuity Pricing," Journal of Pension Benefits, Volume 30, No. 1 (Autumn 2022), click for PDF at 401KAnnuityHub.com

Tamiko Toland and Michael Finke, "How In-Plan Annuities Enable Participants to Turn Savings into Income," Retirement Income Institute, Institute Note (July 2025), click for PDF at 401KAnnuityHub.com

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