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2019 ANNUAL MEETING & EXHIBIT

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Toronto, Canada

Session 064: DC and Other Non-DB Employment Benefit Options Used as Sources of Retirement Income

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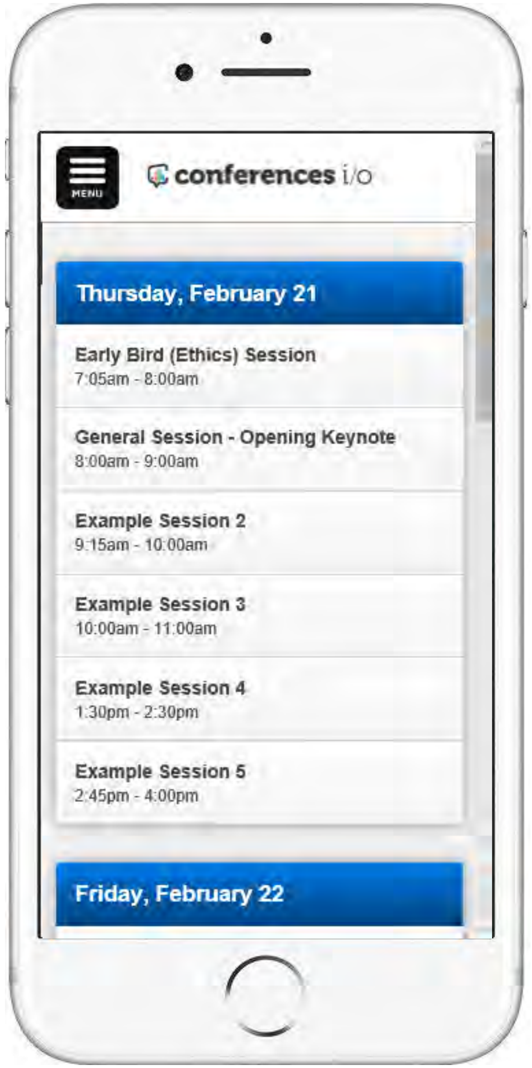

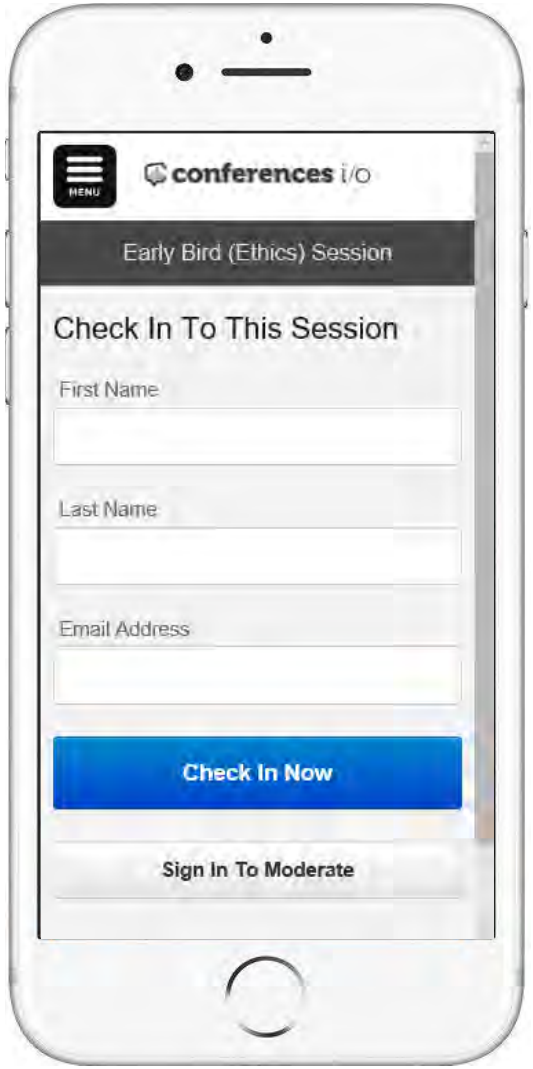

2019 ANNUAL MEETING & EXHIBIT

DC and Other Non-DB Employment Benefit Options Used as Sources of Retirement Income

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October 28, 2019

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Agenda

- Defined Contribution Retirement Programs in the United States
- Defined Contribution Retirement Programs in Canada
- Compare and Contrast

United States

401(k) plans and decline of DB plans

- Initially established primarily at large companies that also had defined benefit plans – though soon smaller companies without DB plans would establish them
- Designed to be supplemental savings to DB plan and not be primary source of retirement income

But DB Plans have declined:

- 2017: Participation in private DB plans at 15% (compared to 38% in 1998)

Ted Benna: Designer of initial 401(k) plan:

"I knew it was going to be big, but I was certainly not anticipating that it would be the primary way people would be accumulating money for retirement 30 plus years later."

401(k) plans and retirement income

Increasing recognition of need for 401(k) plans to provide retirement income in response to decreased prevalence of DB plans

- 2019 Lifetime Income Solutions Survey by Willis Towers Watson:

https://www.willistowerswatson.com/en-US/News/2019/09/more-employers-are-adopting-lifetime-income-solutions-for-DC-retirement-plans

- 90 % of plan sponsors consider it a priority to implement retirement income solutions. But only 30% have retirement income solutions in the plan (an increase from 23% in 2016)
- A separate T-Rowe price study says 64% of 401(k) providers are interested in retirement income solutions but only 23% have implemented

Behavioral Economist Richard Thaler:

“We’ve made good progress on the accumulation phase of retirement saving, but the decumulation phase hasn’t received nearly enough attention. This is unfortunate because the spending-down phase is even harder for individuals to solve, especially since so few people elect to annuitize their wealth.”

-Who better to solve this issue than Actuaries

Higher Education and 403(b) plans:

- Defined Contribution retirement plans in Higher Education: Andrew Carnegie founded TIAA in 1918 to keep faculty out of poverty in retirement
  - Over 60 years before 401(k) plan
- Initially only access to funds was lifetime annuity at retirement
- Annuities have always been offered in 403(b) plans, providing comfort with annuities and annuity driven retirement income. 403(b) plan sponsors are comfortable having annuities in the investment lineup.

“403(b) plan sponsors feel more responsibility for their participants after they retire, so it’s no surprise that they are taking the lead on retirement income tools and solutions.” -BlackRock, 2019 DC Pulse Survey

Pension Protection Act (2006) and recent trends in 401(k) and 403(b) plans

- Pension Protection Act in 2006 applies ERISA to most 403(b) plans (government, non-electing church, and non-ERISA DOL safe harbor plans excluded)
- Created more similarities between 401(k) and 403(b)
- Open-architecture now norm on both 401(k) and 403(b)
- Key provisions include allowance of auto-enroll and auto-escalate features to increase participation in plans
- Qualified Default Investment Alternative:
  - Fiduciary safe harbor for default investments for those auto-enrolled: Primarily filled by target date funds in both 401(k) and 403(b) plan

SECURE Act and retirement income

- Proposed law:
  - Passed the House 417-3
  - Held up in the Senate by two senators for reasons unrelated to the core retirement income provision

Key features

- Annuity safe harbor: Eliminates barrier to including in-plan annuities
- Retirement Income benefit: In addition to showing just accumulation a monthly income projection must also be provided

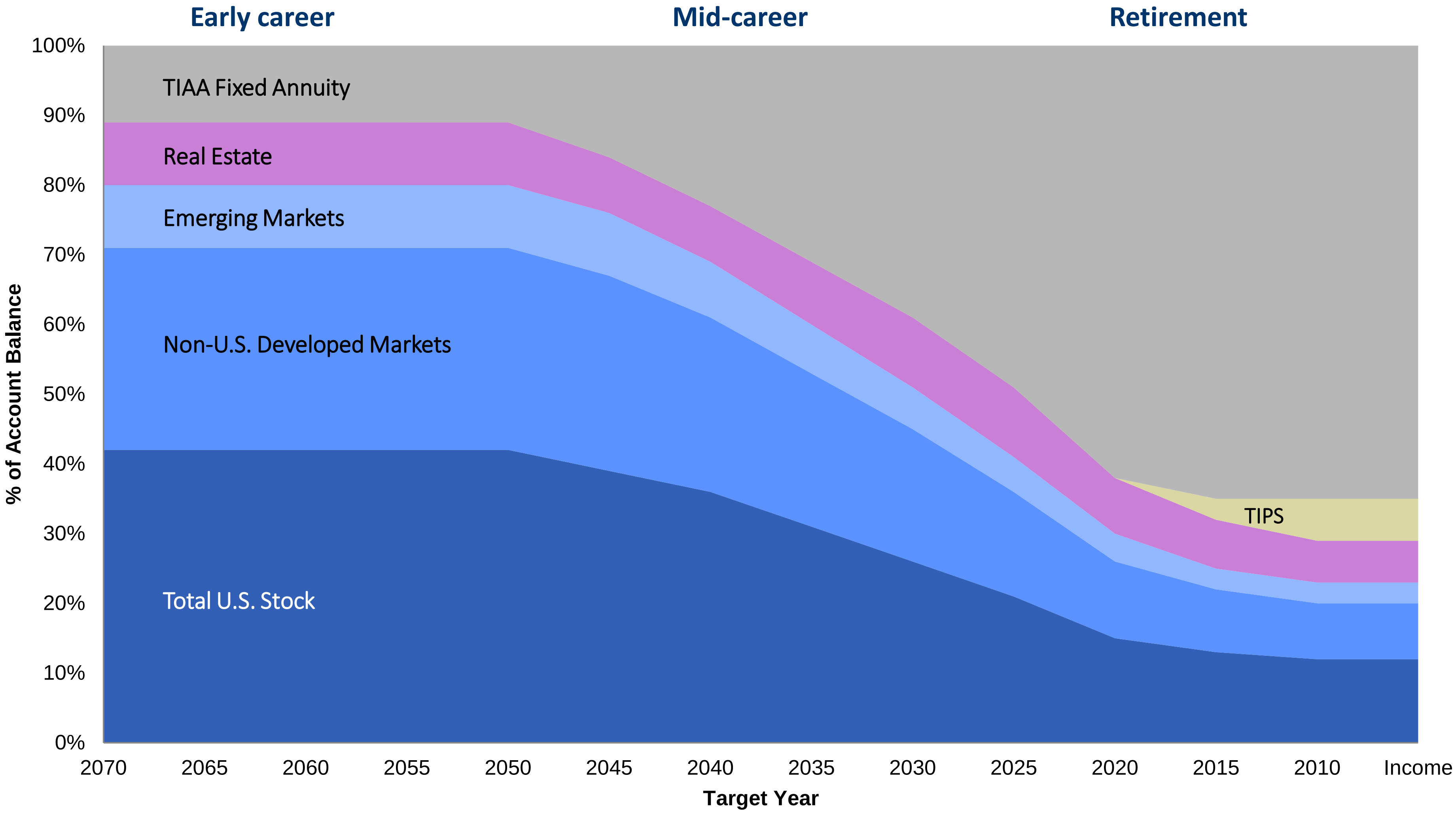
Key Retirement Income Options

- Fixed Payout Annuities:
  - -Provides post-election longevity pooling
  - -Primary option in 403(b) plans
  - -Also available in IRAs, but participants on their own to figure out options
- Variable Income Annuities: Available in many 403(b) plans (CREF)
  - -Less Utilization than fixed payout options
- QLAC: Up to 25% of accumulation (up to $130,000) can be used to buy an annuity that starts as late as 85 under updated tax regulations
  - -Significant longevity credits, especially if cash refund option not selected
  - -Recent innovation. Usage has been low thus far and primarily in retail IRA market
- Guaranteed Lifetime Withdrawal Benefits:
  - -Provides longevity protection and liquidity
  - -Higher fees than other options
- Self-managed retirement withdrawals: Most common 401(k) option today.
  - -Default target date funds are available and default option, but participant must figure out withdrawal strategy beyond Required Minimum Distributions
  - -No longevity pooling

A default retirement income solution

- A custom portfolio that includes a mix of a variety of investments – can include mutual funds, CITs, annuities
- A fixed annuity is included as a portion of a participant's investment, generally increasing the allocation as the participant nears retirement
- Combines the benefit of an all-in-one target date fund and the lifetime benefit of a fixed annuity
    - Creates partial annuity payment option for plan participants using behavioral economics principles

A Custom Portfolio Example:



Healthcare sources

- Dedicated sources of income for healthcare costs in retirement
- Tax free if used for healthcare
- Won’t affect calculations for Medicare part B and D premiums

Retiree health (DB and DC, if any)

HSAs

Canada

Canadian Retirement Landscape

- Increasing shift to Capital Accumulation Plans (CAPs) in private sector
- New set of risks, challenges and considerations for both members and sponsors
- CAP programs beginning to mature – focus on decumulation

New Challenges

- In addition to the challenges during the accumulation phase, members of CAP programs are faced with the complexity around converting an asset value into retirement income sufficient to meet their retirement needs and longevity

Options to Canadians

- Common available options to members with a CAP balance at retirement are:
  - Purchase an individual annuity
  - Transfer to a variety of “income funds” (RRIF/LIF/LRIF)
  - Variable benefits directly from registered plans (subject to legislation)
- Other possible alternatives that may be viable in the future, but require changes to current rules

Options to Canadians

- Individual Annuity
  - Longevity protection, but at a price
    - Expensive – no pooling advantage
  - No flexibility
  - At the mercy of market prices at retirement

Options to Canadians

- Transfer to RRIF/LIF/LRIF
  - Member retains investment and longevity risk
  - Flexibility

Options to Canadians

- The following table shows the minimum/maximum LIF withdrawal rates (Ontario), and the draw down of a $1 million account balance assuming the maximum is withdrawn each year
- The account is assumed to grow at 1% per year
- Assumed to start withdrawing at age 55

Options to Canadians

Age	Balance (BOY)	Withdrawal	Min Withdrawal Limit	Max Withdrawal Limit
55	1,000,000	65,069.68	2.8571%	6.5070%
60	746,958.96	51,194.11	3.3333%	6.8537%
65	545,837.00	40,282.11	4.0000%	7.3799%
70	385,434.58	31,701.83	5.0000%	8.2250%
75	256,931.83	24,956.99	6.6667%	9.7135%
80	153,374.63	19,659.15	10.0000%	12.8177%
85	69,257.71	15,510.88	20.0000%	22.3959%
86	54,361.85	14,800.35	25.0000%	27.2256%
87	40,031.12	14,128.34	33.3333%	35.2934%
88	26,232.46	13,498.25	50.0000%	51.4563%
89	12,929.04	12,929.04	100.0000%	100.0000%

- 75% of funds disbursed by age 75
- 100% withdrawal by your 90th birthday (by law)

Options to Canadians

- Variable benefits directly from registered plans
    - Simplicity for members – same administrator during accumulation phase
    - Reduced fees, from pooled asset management
    - Prepackaged investment choices; default options
    - Member retains longevity risk

Options to Canadians

- Variable benefits directly from registered plans

Created with mapchart.net

- Currently allowed everywhere except for Ontario, New Brunswick and Newfoundland
- Ontario legislative framework in the works, but not currently available
- **Requires plan to adopt provision for variable benefits**

Options to Canadians

- Variable benefits directly from registered plans
  - Sponsor may be apprehensive to adopt variable benefit provisions
    - Increased governance requirements, risk and cost
    - Multi jurisdictional issues

- Currently no viable options that address all of the key challenges and risks of CAP members:
  - Cost (investment fees, individual annuity pricing)
  - Longevity
  - Flexibility/retaining control of money

Other Potential Solutions

- Variable Payment Life Annuity (VPLA)
  - Current Liberal government proposed plan for VPLAs in budget for 2020 tax year
  - Paid directly from registered plan (DCPP/PRPP)
  - Provide income for life, similar to an annuity, but payment changes for investment return and survivorship
  - **Risk is pooled**
  - Working model already in Canada – University of British Columbia has grandfathered VLPA before rule change in 1988
  - Seems like desirable solution, but far from implementation?
    - Numerous complicated issues to work through

Other Potential Solutions

- Advanced Life Deferred Annuities (ALDA)
  - Current Liberal government proposed plan for ALDAs in budget for 2020 tax year
  - Not possible to commence pension income past age 71 under current Income Tax Act (ITA) regulations
  - Idea for providing longevity protection, ie. deferred annuity commencing at age 85 for example
  - Cost Effective
    - At age 65, a deferred annuity commencing at age 85 can cost as little as 10% of an immediate annuity providing the same benefit

      Immediate factor at age 65 ~ 12
      Deferred factor from age 65 to 85 ~ 1.25

      (Assumes an interest rate of 6% per year and Canadian Pensioner Mortality Table)

Compare and Contrast

Comparison: Canadian and US retirement programs

- Although the terminology varies, there is much in common between the programs for the two countries
- Canada has advanced farther in considering variable payout programs within registered plans. US application of this concept very limited.
- Canada's maximum limit on annual payments from the individual account (RRIF, LIF, LRIF) helps encourage spreading payments over time. No comparable provision in the US.
- US has more options for retirees to retain funds within employer sponsored program with greater investment flexibility
  - Open architecture allows participants to choose between investment managers and invest in specific funds of their choosing while leaving their funds in the Plan

Comparison of Payout Features

Feature	Canada		United States		Combine?
	Current	Future	Current	Future	
Transfer money to tax favored individual account	Yes		Yes		
Limits on payout from individual account	Yes – min and max		Yes - min		
Retain money in plan	Yes*		Yes		
Purchase annuity outside of plan	Yes		Yes		
Purchase annuity from the plan			Uncommon	SECURE Act	
Deferred annuity		Proposed	Yes - QLAC		
Variable life annuity in plan		Proposed			

* Not available in New Brunswick and Newfoundland; Approved, but not yet available in Ontario

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