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Aging and Retirement

Insights on Spending and Asset Management in Retirement

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Insights on Spending and Asset Management in Retirement

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CONTENTS

Introduction **4**

Major Observations **4**

Major Findings from Formal SOA Studies **5**

The Conversation **5**

Spending In Retirement: What Research Shows **8**

QLACs and Behavior **11**

Conclusion **16**

About The Society of Actuaries **17**

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Introduction

In late 2018, participants of an Society of Actuaries (SOA) listserve focused on post retirement needs and risks engaged in an online conversation on spending in retirement, asset management and the use of Qualified Longevity Annuity Contracts (QLACs), which are deferred annuities that start making payouts to the annuitant at the higher ages, such as 85, and sometimes called longevity annuities. The listserve was established by the SOA Committee on Post-Retirement Needs and Risks (the Committee), which is part of the SOA Aging and Retirement Strategic Research Program. The conversation participants represent a broad range of expertise on these and other retirement and aging issues.

The inquiry sought the participants' views and experiences on these important retirement issues. The comments were purely anecdotal but revealing in terms of how personal experiences have shaped their ideas about trends that may be emerging in this field.

Several points that came up during the conversation, selected for their insight and their general interest to the retirement community at large. The Committee presents this conversational material as a supplement to the extensive retirement research studies the Committee has previously published. Reports can be found at https://www.soa.org/research/topics/aging-ret-topic-landing/.

Major Observations

The conversation opened with questions about overall trends among retirees and advisors as follows:

- Is anyone personally spending down assets in retirement (systematically or not)?
- Is anyone helping someone else spend down their assets in retirement?
- Has anyone personally purchased deferred longevity insurance?
- Has anyone helped someone else purchase deferred longevity insurance?

Some key observations to emerge from the conversations involved two topical areas: 1) spending in retirement and 2) QLACs. QLACs, as noted, are deferred annuities designed for use in planning for longevity needs. Note these observations are a summary of the views of conversation participants and not official views of the Committee on Post Retirement Needs and Risks nor other SOA entities.

Spending Overview

- **Variety:** People vary in their approach to spending in retirement and vary greatly in how much they consider the longer term.
- **When spending declines:** Average household spending declines at the high ages except for health care costs.
- **Much focus on short-term cash flow planning:** A common form of planning is short-term cash flow planning, rather than more comprehensive planning.
- **Formal processes not widespread:** Some people have a formal process such as a structured spending budget but others do not have any formal process.
- **Need for simplification grows with age:** It is critical for some households that financial management be simplified before they reach very high ages.
- **Lack of analysis about future finances:** Many people do not have access to a thorough analysis to tell them how likely they are to run out of money.

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QLAC Overview

The QLAC type of deferred annuity starts paying out benefits at a high age, such as 85, and usually not before. These annuities enable a person to buy insurance for living long without giving up control of their other assets that could be used for the period up to age 85 or the start date of the QLAC payments.

Here are some participant views on these fairly new products:

- **Overview:** QLACs help with the management of longevity risk and are a relatively recent market innovation so it is too early to tell how much they will be used in the long-term.
- **Expected use:** QLACs will be used by people who do very long-term thinking and not many are in the payout period today.
- **Financial questions:** QLACs increase income at high ages. They do not automatically smooth income when combined with other assets.
- **Beneficiary risk:** As with any financial instrument or arrangement that is not paid out until a number of years after purchase, there is a risk that they can be forgotten.
- **Employer plan issue:** Employers have found relatively few elections of options that combine multiple types of payouts in one option.
- **Behavioral aspects:** Behavioral economics is helpful in understanding the issues.

Major Findings from Formal SOA Studies

Those overall observations correlate with insights from previous research the Committee has conducted into how retirees change their spending over time and how they think about using their assets to support themselves and generate lifetime income.

Some major findings include:

- **Limits on spending:** Many retirees try to limit their spending to regular income they receive. They are willing to reduce expenses to match income, but unusual expense items may require asset withdrawals.
- **Hold onto assets when possible:** Many retirees prefer to hold onto assets and limit withdrawals to the annual Required Minimum Distributions (RMDs) they must take from their tax-qualified retirement savings plans generally starting after age 70.5. Assets also serve as an emergency fund, as there is often no other specific emergency fund.
- **Handle financial shocks when they happen:** The major method of dealing with risks and shocks, such as major repairs and medical emergencies, is to handle a shock when it happens rather than planning in advance.
- **Household expenses decline:** Except for health care expenses, most types of household spending decline during retirement.

These findings have emerged from SOA's biennial *Surveys of Post-Retirement Risks and the Process of Retirement* as well as from SOA focus groups and in-depth interviews. Another source are various SOA papers that document the decline in expenses and patterns of asset change discussed in the SOA studies—these papers are based on analysis of the *University of Michigan Health and Retirement Study (HRS)*, which is supported by the National Institute on Aging and the Social Security Administration.

The Conversation

The remainder of this document includes excerpts from the online discussion categorized by topic. The excerpts provide insight into the range of approaches and varying perspectives of the participants and reflect their wide-

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ranging areas of expertise and experiences. The discussion also includes some detailed findings from relevant studies.

Participants' comments are indented and appear in italics. The content reflects very light editing for grammar and spelling, with names and identifying details withheld for the sake of privacy.

Overriding Message: People are Different

> *An important point that can be overlooked is that there is a range of financial situations and a range of personality types, as well as a range of expectations and financial/social tolerances (and relative preference for current and future consumption/bequests, i.e. personal long-term discount rates). There is no such thing as an average or median person/family situation.*

Lifetime Income and Spending: What Committee Members Said

The Committee members were asked if they personally have a plan. A number are retired or near retirement age.

> *I am personally systematically spending down assets in retirement with my tax-advantaged retirement accounts—Thrift Saving Plan and 403(b)—using the RMD as recommended by Steve Vernon* et al.*'s study for SOA. So far in 2017 and 2018, the spend-down following the RMD is less than the income earned by these funds. I also have a Federal Retirement pension systematically sending monthly income from the CRSR plan based on 40 years of service. In addition, I have a small benefit from the Social Security Administration. I am 72 and retired. My wife is also 72 and receives a SS benefit but continues to work part-time.*

Here is another approach:

> *Every January, we sit down and calculate our Actuarial Spending Budget for the upcoming year. It is very much an actuarial valuation process. Our actuarial spending budget anticipates a relatively small bequest, so I suppose you could say that our spending budget anticipates that we will spend down our assets. However, we don't necessarily spend our spending budget each year, although we do track how much we spend.*

Here is a third approach:

> *I am not an actuary. I believe that I am part of a much larger group and not necessarily less responsible. Just different.*
>
> *I know roughly how much I have in the money market account (settlement account at Vanguard) on which we write checks and which pays credit card balances (in full) and other recurring charges such as electricity and water bills. My wife draws on it too, and we do not coordinate. We just have more than enough to be sure that checks do not bounce.*
>
> *I know where I stand in spending by watching my money market balance over time.*
> *Salary goes into my regular bank checking account and moves to my tax-free account from which I transfer to my settlement account as needed. RMD goes into my tax-free account, etc.*
>
> *I paid my mortgage balance years ago because I did not want to be bothered with it. I did not consider the alternative of paying the mortgage gradually and investing the money in the stock market. It is not that I don't care about money. I can stay on the phone for an hour to retrieve $10 charged to me in error.*
>
> *My balances are much larger now than when I was young, but my method is the same.*

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Does it seem irresponsible? Is there a selection bias whereby some become professors and others become actuaries? I can see myself as a physician or a lawyer doing litigation or deals, but not as an actuary—I have no patience for details.

How much does personality affect how we handle money? Is there one best way to do that?

Here is a fourth approach:

I have no formal long-term plan either. I just know that I consume income first, then regular capital, then bequest capital, then rely on my children. So, I do have a long-term plan, even if not on an excel sheet. I am not alone in that.

Here is a fifth approach:

We do not have an explicit spending budget. In some years, quite a lot of money goes out to help family members who need help. We carefully track assets and have very detailed statements of assets at the end of every year.

Before making a significant purchase, we ask the question: How will this improve my life? If we can't say it will improve our lives, we skip it. We also review expenses carefully at the time of preparing tax returns. If we are satisfied with overall progress, we do not worry on a week-to- week basis. So far, it has worked out fine over more than ten years of retirement.

Two participants reported they have deferred annuities that begin making payouts at high ages (often age 85 or over). These are the QLACs mentioned earlier; the products are also known as longevity insurance. The conversation generated much discussion about QLACs. A section on these products appears later in this report.

A Personal Story

One participant outlined his plan step by step:

I've given a lot of thought to retirement, both professionally and lately for our own retirement. I'll be age 65 in a few weeks, and my wife attains age 65 this December. Here's what we are doing. I left my career job at age 53, but plan to work until age 70 at work that I enjoy and find fulfilling. I'm making much less money now but that's ok, the kids are off the payroll.

We plan to do the following:

- *Delay my SS until age 70.*
- *Start my wife's earned SS at her FRA. Take advantage of the trick that lets me take a spouse's income on her earned SS without compromising my delayed retirement credits.*
- *Start my pension when there was no longer an early retirement reduction factor.*
- *For 401(k) and IRAs, start the RMD at age 70-1/2.*
- *For savings outside 401(k) and IRAs, invest significantly in low-cost stock index funds and keep the principal intact. Spend the dividend income.*
- *Most likely we will not buy any other annuity. If we didn't have the pension, we would have purchased a low-cost SPIA with some of our savings to cover our basic living expenses.*
- *We paid off the mortgage as a de-risking strategy. To do this, we took money invested in fixed income to pay off the mortgage—the fixed income investments were earning a lower rate than the mortgage interest rate.*
- *Buy a Medigap Plan G.*

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- *For LTC, we are holding the principal intact of our non-401(k) savings and are keeping the house mortgage-free. If we need to, eventually we'll spend principal and then tap the home equity to pay for LTC. If not, these assets will create a legacy for children and charities.*
- *Be diligent about exercise, good nutrition, and adequate sleep. Keep our weight at healthy levels.*
- *Be on great terms with family and close friends, helping them as needed.*
- *Nurture a robust social portfolio.*

This creates enough income to help adult children, contribute to grandchildren's college funds, donate to charity and travel—all discretionary expenses. If necessary, we'll cut back this discretionary spending. We'll have our basic living expenses covered with a pension and SS. While we are quite fortunate in our circumstances, I believe that many middle-income people could use these ideas and variations to manage their finances in retirement.

Spending In Retirement: What Research Shows

The Health and Retirement Study (HRS) is a national longitudinal data base of older Americans who are interviewed every two years. Analyses of the HRS provide a picture for the entire population. An economist observed about the HRS research: *"Couples spend approximately their after-tax income and so wealth trajectories are approximately flat. Singles spend more than their incomes and so their wealth trajectories have negative slopes."*

Work from the Employee Benefit Research Institute (EBRI) using the HRS database indicates that while individual behavior varies, overall household spending goes down by age group, except for medical care.

The table below shows how mean household health expenditures are increasing from age 65–74 to higher age groups while most expenses are decreasing. A decrease in household size contributes to the decreases but does not explain it.

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Table 1
Mean and Median Household Spending in 2011
Adjusted to 2013 Dollars by Age Group

	Age 65–74		Age 75–84		Age 85+	
	Mean	Median	Mean	Median	Mean	Median
Home	$18,720	$12,642	$14,732	$10,805	$13,111	$8,781
Food	4,526	3,982	3,994	3,228	2,520	2,152
Health	4,383	3,104	4,624	3,109	6,603	2,814
Transportation	5,169	4,025	3,666	2,794	1,972	1,241
Clothing	1,311	724	950	569	888	434
Entertainment	4,300	2,380	3,277	1,655	1,609	714
Other	3,583	1,148	3,565	1,034	3,188	734
Total	$42, 805	$34,036	$35,315	$29,884	$30,610	$22,263

Source: Figure 2 from EBRI Notes, Sept. 2014 – *How Does Household Expenditure Change with Age for Older Americans?*

Society of Actuaries Research

SOA surveys with people age 85 and over also show spending reductions by age. The age 85 and over retirees tend to be frugal and seem willing to manage their spending to fit their income. Some highlights include:

- When asked about how their spending habits compare to their income, only about one in eight (12%) report spending more than they should, and only 3% report spending a lot more than they should.
- About a quarter (23%) report spending less than they should, with females (28%) far more likely to say this than males (13%).
- The biggest factor behind these findings is that most respondents considered themselves to be at least somewhat frugal—a quarter very frugal (25%) and a half (51%) somewhat frugal.
- Widows (80%) are more likely to be frugal than others (64%).
- Frugal behaviors seem to have lasted a long time with close to half (48%) reporting being just as frugal as they were 20 years ago and only one-third (34%) reporting being more frugal.

Many of the research findings are in contrast to traditional thinking about retirement planning which often focuses on maintaining the pre-retirement standard of living. That thinking exists even though people recognize the existence of inflation and often increases in medical costs.

Some highlights of the SOA research results on spending include:

- Most respondents to the survey of adults age 85 and over reported they were spending the same (34%) or less (38%) than they did 10 years ago, with women (44%) more often saying that they spend less than men (28%).
- When compared to 10 years ago, most respondents reported spending the same or less in several key areas. A large majority (74%) said they were spending less on travel and a majority (60%) reported spending less on entertainment.
- Even when it comes to medical costs, only a little more than one-third reported spending more (37%).

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- A plurality reported spending about the same on housing (44%), but more than one-third claimed to spend less (35%).
- Only about one in five claimed to spend more on getting assistance in their daily lives.
- The adult children reported a majority (54%) of their parents spends more on medical care, but this is a less healthy group.

The retirees often voiced the philosophy of paying regular expenses monthly and unexpected expenses as they occur. They indicated this works out quite often, but not when there is a major long-term care need.

The survey and some interviews indicated family members are financially helping a minority of the older retirees, with 14% of adults surveyed saying they are getting financial help from their families, and 50% of the children surveyed say they are helping their parents. Of the 50%, 11% say they are helping a great deal, 18% to some extent, and 21% a little.

Behavioral Issues

The research of the Committee on Post-Retirement Needs and Risks has consistently shown many people are thinking short-term and not planning long-term. They are not preparing long-term calculations, and with the exception of health care, most of them are not focused on longer-term risk management. It is well known many people are not making decisions based on longer-term economically based analysis.

In the online conversation, several participants made comments on behavioral issues.

One participant said:

> *The behavioral aspects are critical. I heard Dan Ariely speak yesterday morning at the Investments & Wealth Institute annual conference.*
>
> *Has the industry consulted with him, or others like him, on product design? It seems the problem is these products are built by economists (no offense to any on this string) who expect humans to make economically rational decisions. That is not how we make decisions. If they can design choices that get people to take other actions (organ donation, switching to generic pharmaceuticals, auto-enrollment in retirement plans) it seems with some design and experimentation the right set of choices could be designed that get people to buy lifetime income.*

Another response:

> *I agree with others that behavioral finance experts should be more involved in the product design process.*

In reply to a question on whether someone with $800,000 would spend $500,000 to buy a $35,000 annuity while keeping $300,000 in savings, one participant had the following thought:

> *A man with $800,000 considers himself almost a millionaire. A man with an annual income of $35,000 considers himself barely middle class. Quite a descent in status.*
>
> *We are still thinking about the issues within standard life-cycle theory, where people care only about utilitarian benefits of wealth and really mean it when they say all they want is not to run out of money. I don't believe that. If it were so, people would have been eager to buy annuities. We need to think about the issues within behavioral life-cycle theory.*

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Maybe the problem we are trying to solve with financial instruments is not to be solved with financial instruments. Maybe we should stop banging our heads against the instruments wall and realize that people are not stupid when they reject those instruments.

People care about expressive and emotional benefits of wealth in addition to utilitarian benefits--We derive social status and pride from looking at an account with an $800,000 balance. (This is the modern version of people who caress their gold coins before they go to bed each night.) Moreover, people actually have a plan--Spend income first, then dip into regular capital (e.g. saving account, IRA) if we need, then dip into bequest capital, if we must. Then rely on family.

Recall the woman who said that she does not know what to do if she needs nursing care. In fact, she does know. She says that her children would not abandon her.

QLACs and Behavior

I think that deferred longevity insurance is a very tough sell behaviorally—similar to an immediate fixed annuity but different too. For instance:

- *Immediate annuity – If someone has $800,000, they like to be a person who has $800,000 and would rather be that person than a person who has $200,000 and an annuity contract for $35k a year.*

- *Deferred longevity insurance – If someone has $800,000, the idea of spending $100k on $35k of income that starts when they turn 85 and are too old to enjoy it doesn't seem appealing. Plus, anyone who does the math will notice that it's only $20k on an inflation-adjusted basis. Since people don't care to spend down their money anyway. Why would they want a product that helps them spend it down?*

Here is another quote on QLACs and behavior:

The challenge is that QLACs and any other financial products aimed at the long-term will only be useful for people thinking about the long-term and building a portfolio to address long-term issues. Until people start to focus longer term, none of these products will get fair consideration. Any ideas to increase longer-term thinking will be most helpful.

Where Advisors Fit In

One advisor provided anecdotes from experience:

Yes, we help people spend down their assets. Here are examples of 5 clients (anonymously) and how spenddown is occurring.

- ***Moderate spenddown client:*** *In real terms, this client is spending down. The spike near the end is due to a deposit from a planned real estate sale.*
- ***Spenddown–single widow:*** *This is a single woman in her 80s. She received an influx of assets midway through due to the settlement of a lawsuit on assets owed to her from a business her husband had been involved with.*
- ***Spenddown in real terms client:*** *This couple retired about December 2006. The increase in the resources is their 401(k) rollovers. In real terms they are spending down assets.*
- ***Dramatic spenddown client:*** *This person retired at a bad time and spent far more than projected. A large portion of the spending is due to supporting an adult child who lost their job during the recession.*

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- ***Planned Spenddown with Social Security delay client:*** *This planned spenddown was combined with a delayed SS start date.*

Note: These examples are quite different from many situations in the SOA focus groups and interviews. A dramatic difference is longer-term thinking and a longer-term planning horizon vs shorter in the focus groups

A Plan Sponsor Perspective

From a plan sponsor perspective, more than a decade ago, our DB plan:

- *Had a "pop-up" election (lowering the initial benefit, popping up at a later date, typically to coordinate with short-term, deferred compensation installment payouts),*
- *Had a "Social Security level income option" designed to transition individuals from age 55 (or later) to age 62 and Social Security benefit commencement, and*
- *Considered adding a "Social Security level income option" designed to transition individuals from age 55 (or later) to SSNRA (65, 66, 67) or to age 70.*

Few elected these payments, so I had no luck adding a level income payment to age 70. As of today, I believe most of these benefits rights and features were prospectively eliminated, "worn away".

I believe plan sponsors would be interested in a non-annuity, in-plan payout option for their individual account retirement savings plans. The study jointly sponsored by the Society of Actuaries and the Stanford Center on Longevity authored by Steve Vernon, Joe Tomlinson, and Wade Pfau [Optimizing Retirement Income by Integrating Retirement Plans, IRAs, and Home Equity] *work suggests this would be of particular value to middle-class retirees.*

I may not understand it completely, but here is how I thought it might work (or perhaps one of many alternatives):

- *Almost all individual account plans already have a default form of payout - installments commencing in accordance with minimum distribution requirements (RMD).*
- *This would amend the plan to add a default form of payout where individuals commence prior to RMD date.*
- *We have mandated default forms of payouts in pension plans—Qualified Joint and Survivor Annuity (QJSA) for married individuals, Single Life Annuity (SLA) for non-married—so, I'm hoping this doesn't trigger any compliance concerns in a profit sharing setting like the 401(k), as the participant would generally (depending on plan provision) be able to opt out, stop payments (if prior to RMD), change the amount, accelerate payout or cash out,*
- *The amount paid between benefit commencement and RMD would be the monthly amount (readjusted as necessary) that would smooth out income from the combination of Social Security and the 401(k) until some target age (85, 90, 95?).*
- *The amount paid from the 401(k) upon reaching RMD date would be based on the RMD requirements.*
- *Social Security would be assumed to commence at age 70, and*
- *The default would come with an appropriate investment Qualified Default Investment Option (QDIA) to anticipate the cash flows—perhaps rebalancing the account after every monthly payment.*

So, when modeling this, the participant would see a stream of payments from the selected commencement date, where at age 70, Social Security would start and at RMD date, RMD payments would start (based on the Uniform Table and the projected residual balance). It might be a smooth, ever increasing income stream. It might be a start and stop income stream should the participant run out of 401(k) monies prior to age 70.

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By modeling this at, say, age 50, without projecting any future contributions to the 401(k), the participant would get a clear picture of where she stood in terms of preparation. The model should only require a participant to supply her estimated Social Security benefit at normal retirement, her date of birth, and her 401(k) account balance. Up to all of you how much you want to enable the participant to vary interest rates, inflation assumptions, mortality, etc.

With others, I've toyed with the option to introduce a "disability" benefit triggered by the inability to perform two or more activities of daily living[1] (ADL)s—a "pop-up"of income coincident with meeting the "2 ADL""requirement. We gave this some significant thought because of tax code changes which extended tax-deductible medical treatment to long-term care (LTC). So, if the individual itemized, the person might capture some of the tax preference, lowering the out-of-pocket cost of LTC services.Today, after the Tax Cuts and Jobs Act of 2017, fewer retirees are likely to itemize, even if they have noticeable medical expenses. But, I never found anyone who was confident in the pricing. We even considered a "variable annuity" concept, where the benefit would vary up or down based on the overall claims experience among those who elected the LTC option. We once had a variable annuity where a portion of the DB benefit reflected investment performance, up or down. No one was interested in placing the plan at risk, or in re-introducing an up or down income stream.

[We're] Hoping to innovate, to create an option that would deliver enhanced value to participants, but avoid triggering substantial compliance challenges or adding new risk exposures for the plan sponsor/fiduciaries."

Views on QLAC and Their Future

As noted earlier, a QLAC is a deferred annuity with payments starting at a high age, such as 85, and usually no benefit before that. It enables a person to buy a future income stream via an annuity that begins payouts at the upper ages. As such, it serves as insurance against living long without giving up control of the assets.

The U.S. Treasury developed QLAC ideas in 2012-2014. The goal was to address some of the behavioral obstacles to demand for annuities in the 401(k) and IRA markets by providing a particularly target-efficient means of managing longevity risk for those who have some meaningful savings.

The hope was the QLAC would be an easier "value proposition" to sell to participants than single premium immediate annuities (SPIAs). The product would cost only roughly 15% of an account balance to buy meaningful protection against burning through assets if an individual lives past 80 or 85. Two anticipated results would be less of an inclination by retirees to hoard/underspend.

In the SOA's online conversation, the discussion and intermediate comments triggered a request to hear more thoughts from participants about QLACs and the efforts to improve them. Following are some examples:

A personal perspective

My QLAC is what allows me to sleep well without worry about living to 100 or later—family genetics suggest at least early 90s—and being able to fully budget spending only to 85 is a big assist in spend down certainty, given how we are invested.

Another personal perspective

[1] Activities of Daily Living (ADLs) are functional capabilities such as toileting, transferring, eating, dressing, etc. ADLs are used to measure functionality in people with limited functions and inability to perform two or three out of six ADLs. This serves as a trigger to measure eligibility for long-term care benefits in many long-term care insurance policies.

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And yes, I did buy a QLAC several years ago. No regrets. Because we assume conservative longevity planning periods, buying a QLAC increased our current spending budget.

SOA Sponsored Research Into QLACs

The SOA, in partnership with the Stanford Center on Longevity, sponsored a series of studies on lifetime income. QLACs were Phase 3 of the study "Optimal Retirement Income Solutions in DC Retirement Plans."

Some of the discussion by Committee members asked why the study did not more enthusiastically support QLACs. Joe Tomlinson, one of the authors responded:

My recollection is the main problem we had with QLACs involved complexities in coordinating between the deferral and payout phases. Use of the products seemed more appropriate for clients working with competent advisers than for more "automatic" retirement solutions for 401(k) participants. Also, QLACs didn't seem to provide significant financial benefits over SPIAs.

From a financial standpoint, the first consideration should be optimizing Social Security (typically by deferred claiming) before considering SPIAs, QLACs, or other products to provide lifetime income. I wonder if it might be worth trying to find an effective way to offer inflation-adjusted SPIAs as a way to "buy more Social Security income" if there is a desire for more lifetime income after optimizing Social Security. That way the annuity decision would fit in more naturally when the focus was on increasing lifetime income via Social Security optimization.

I also like the idea of tying in long-term care (LTC). About a decade ago Mark Warshawsky proposed the Life Care annuity that would pay a pop-up benefit if there is an LTC need as determined by claim criteria. But, like many good product ideas, the Life Care annuity never gained much popularity.

A practical issue with regard to QLACS (from an advisor)

I appreciate this vibrant conversation and would like to add a practical planning point I have not yet seen mentioned: Older people have trouble keeping track of their finances. It would be easy for QLACs to go unused.

<u>Background:</u> In our financial planning firm, we make a point of gradually simplifying daily finances for our clients as they age. The goal is that daily financial life will be fully automated or delegated well before cognitive decline becomes operative, and in particular that inflation-protected lifetime income covering fixed overhead expenses will be automatically deposited into the daily checking account, where it will fund fully automated draws for essential expenses.

Automation of daily financial life is helpful, if not critical. Cognitive decline often appears first in one's financial life but is often not noticed in a timely way because finances are private. Ouch. If there isn't an advisor, family member, or trust officer who is watching an older person's daily transactions, finances can badly deteriorate before anyone close to them is aware of the need for assistance. Think of all the stories you have heard of adult children finally getting access to their parents' finances and exclaiming with wonder "It was a mess!" In that context, it will be easy for investors to die without having benefited from their QLAC. Families may not know to watch for the income stream. Insurers have little incentive to proactively keep addresses current. The QLAC owner can easily have moved residences and bank relations several times between QLAC purchase and age 85.

This practical planning point points to a larger issue: Managing finances in old age has become stunningly more complex than it was in previous generations. At the same time, there is a falling away of safe

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support. Most people don't have advisors or trust officers. For those relying on family, it can be problematic. Many have no children or only children who are out of state, busy, estranged, addicted, and/or who are illiterate with respect to basic personal finance, including especially the demands of fiduciary responsibility.

A Word of Caution

Managing finances in old age has become stunningly more complex than in previous generations. At the same time, most people don't have advisors or trust officers and relying on family can be problematic if the adult children are out of state, busy, estranged, addicted, and/or illiterate about personal finances.

—Online conversation participant

When planning investment products for older people, I think we need to keep top of mind that no one may be minding the store as the years go by.

Optimal product design would address these practical challenges of aging as well as the behavioral issues already mentioned.

Reflections on the QLAC Discussion

The conversation about QLACs provides views that the products do not provide an easy path to smoothing retirement income after a systematic withdrawal. But they do provide additional income at a later age when it is likely people will need help. QLACs do not provide long-term care insurance but they can help finance the later years in life for care, housing or other needs.

Some people also have limited deferred payouts from other financial sources so they can fill in gaps in available funds by using those sources in the later years.

The QLACs seem to be a better idea for people who have expertise in managing a post-retirement portfolio or have an advisor than for individuals with little expertise or help.

Another consideration pointed out in the online discussion was that QLACs generally do not offer inflation protection. When facing an uncertain longevity period, that can be an issue. Is it worth paying now for a future benefit that will not keep up with inflation? Individuals, financial advisors and the emerging QLAC providers will need to wrestle with this issue going forward.

Insurers have some pertinent thoughts about QLACs, too. Following is one example:

The product is very risky for insurers, given systematic longevity risk, reinvestment risk and anti-selection risk. Even if it is only one-sixth of the value, it probably has more than one-half of the risk of an immediate annuity for the same amount of income.

Some things that could make it [a QLAC] more appealing:

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- *Variable products with investments in various asset classes. Inflation risk is a big issue and this would help.*
- *Combo products with long-term care. LTC seems to appeal to people more and the right kind of combination might be attractive and also mitigate moral hazard problems with LTC insurance.*
- *Combo products with systematic withdrawal management for the deferral period. Managing money over 20 years isn't that much easier than over a lifetime and people will still not want to spend down.*
- *Find a good marketing approach and the sales force will make it grow."*

Final observation: The online conversation about spending in retirement and possible uses for income products like QLACs did spark some discussion about long-term care and its coverage by Medicaid. Another SOA online conversation discussed this subject extensively. Titled *A Conversation on Dementia and Cognitive Decline*, it is available for download: https://www.soa.org/Files/resources/research-report/2018/cognitive-conversation.pdf.

Conclusion

Many people, even financial professionals, take different approaches to how they spend in retirement and what measures they take to ensure they won't outlive their assets. That is one of the implicit views in this online conversation about retirement spending and QLACs.

Even experts in retirement differ in how they handle finances in retirement. This may be surprising to people who think financial experts agree about how everyone should proceed in these areas or people who believe there is a fix-it-and-forget-it approach for handling retirement finances, whether spending or drawing down income.

The underlying theme of the conversation is that retirement planning and living is an individual experience, and people would benefit from help analyzing the various approaches they might take that will work for them. The strategies people use will work best when reflecting who and where the individuals are now and how they hope to live in old age, socially, financially and in myriad other ways. This will help formulate ways they might work to achieve personal retirement goals.

Some of the participants suggested people need greater simplification in spending and income strategies as the upper ages arrive. This can be further necessitated in instances where there is cognitive decline or reliance on others. The QLACs do have the advantage of simplicity. A person buys the annuity and sets the start date for late in life, ensuring an increase to income at a time when it may be needed most. However, as with other financial contracts, late-in-life individuals may forget they have the annuities or they may change residences one or more times following policy purchase and lose their annuity papers in the process. Further, people who do not know how to factor a QLAC into their other financial arrangements may not make the most effective use of their product.

In general, income planning and arranging intertwine with retirement spending. The conversation reveals older people need to learn as much as they can about both and to find reliable others to help older people when and where needed. Experts in the fields of aging and retirement are looking into these issues and searching for simplified strategies and solutions that may be of assistance.

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