



**Retirement Security
in the 21st Century:**
Guaranteed Lifetime Income





Retirement Security in the 21st Century: Guaranteed Lifetime Income

The Challenge

The Changing Retirement Landscape

- A confluence of demographic, social, and economic trends is changing the nature of retirement in America:
 - **The aging of 76 million Baby Boomers** is placing increasing pressure on the Social Security program as well as on employer-funded retirement benefits.
 - **People are living longer**, and savings have to last through retirements that can last 20-30 years, or more. This is of particular concern for women, who tend to live longer but have lower incomes and retirement benefits than men.
 - **Individuals are assuming more of the risk and responsibility** for retirement saving and income generation. Traditional defined benefit (DB) pension plans in the private sector are increasingly being frozen or terminated; virtually all replacement and new plans are defined contribution (DC) plans, such as 401(k)s.
 - **Historically low personal savings rates**, coupled with the general insufficiency of DC plan savings, mean many retirees will have to consider alternative sources of retirement income, such as working in retirement or tapping into home equity.
 - **Healthcare expenses** are rising more quickly than the general rate of inflation. Funding post-retirement healthcare is looming larger as a threat to individuals' retirement security.

Shift in responsibility for retirement security

- The shift from DB to DC plans has shifted much of the burden for retirement security from employers to individuals.
- In contrast to DB plans, where the employer generally bears all the risk and responsibility, most DC plans place responsibility on the employee to decide to participate, save adequately, invest appropriately, and, at retirement, determine how to make the nest egg last for life – while managing the risks that go along with that.
- The retiree in a DB plan usually receives a pension check every month for life.
 - Traditionally, the employer pays a lump sum to an insurer; in return, the insurer promises to pay the retiree a monthly amount as long as he or she lives – sometimes for as long as a beneficiary lives as well, and sometimes with a number of years guaranteed. (In some cases, the employer may self-insure this obligation.)



- A retiree in a DC plan, however, has a sum of money that he or she must decide how to use in retirement.
 - Retirees are typically ill-equipped to manage the funds so as to neither prematurely exhaust nor excessively hoard their funds.

Americans' reluctance to annuitize

- Annuities are the only products that can turn DC assets and personal savings into *guaranteed*, DB-like retirement income.
- Americans have traditionally been reluctant to annuitize their savings, although annuities are available to individuals in the retail marketplace, and sometimes through their DC plans.
 - Employer sponsors of DC plans generally don't make annuities available to plan participants as a distribution option.
 - It is burdensome for the plan sponsor, both administratively and from a fiduciary risk perspective. It is much easier for employers to simply give a participant a lump-sum check.
 - There is little demand by employees. Even when employers offer annuities, only a fraction of American workers elect this distribution option.
 - In the retail market, among the individual investors who have chosen annuities as investment vehicles, fewer than 1% annuitize the assets that accumulate within these vehicles to create a guaranteed income stream.*
- The reasons for this reluctance to annuitize include concerns about cost transparency and product complexity, as well as behavioral deterrents such as:
 - Loss of liquidity and control – People are reluctant to give up access to and investment control over their hard-earned nest egg, even for the guarantee of income for life. This emotional hurdle is significant – in contrast to the way they view Social Security and DB plans, there is a stronger feeling that the money they have managed in DC plans is “theirs”; irrevocably handing the money over in exchange for a stream of payments is not easy.
 - Potential loss of account value upon death – Many people are uncomfortable with the notion that any account value that remains upon the death of an annuity income recipient goes to pay others' annuity benefits, rather than being passed along to heirs. They view this risk pooling, which is necessary for traditional annuitization, as a gamble they are unwilling to take, even though they readily accept the concept of risk pooling when it comes to auto, homeowners, and life insurance.

*LIMRA, “The 2006 Individual Annuity Markets: Sales and Assets,” November 2007.



The Proposed Solution

- Prudential applauds and has been very supportive of the provisions in the Pension Protection Act of 2006 that paved the way for the more widespread introduction of autopilot features in DC plans as a means to increase participation and savings.
 - Leading academic research in the field of behavioral finance has demonstrated the power of “automatic” default provisions that put inertia to work to participants’ advantage.
- However, as Baby Boomers begin to reach retirement, they are faced with a new challenge: finding ways of replicating the guaranteed lifetime income feature of DB plans in an increasingly DC world.
- The logical next step in creating more DB-like outcomes is to extend the DC autopilot concept from the *accumulation* phase to the *payout* phase.
 - Automatically converting at least a portion of DC plan dollars into guaranteed lifetime income would help provide protection against the longevity, investment performance, and other risks that threaten Americans’ retirement security.
 - Creating streams of income through DC plans can be especially beneficial for women. The life expectancy assumptions used to calculate lifetime payments are gender-neutral in DC plans, whereas in the retail market, all other things being equal, annuities are more expensive for women than for men, because women are expected to live longer. Although men may benefit from more favorable underwriting in the retail market, that advantage is generally thought to be offset by the lower fees available for lifetime income products within DC plans.
- Lessons from behavioral finance can be further applied to help create more certain retirement income outcomes in both the DC and individual retail markets by providing economic incentives to create guaranteed lifetime income.
- However, given Americans’ reluctance to annuitize, the solution lies in a more contemporary approach to guaranteed lifetime income that does not require the rigidity of traditional annuitization: a new generation of variable annuities with guaranteed lifetime withdrawal benefits.
 - These programs were elected on over 80% of individual variable annuity sales, and are starting to become available through DC plans as well.**

**LIMRA, 1Q 2008.



The New Generation of Variable Annuities With Guaranteed Lifetime Withdrawal Benefits:

A New Approach to Guaranteed Lifetime Income for Today's Retirees

Guarantees Lifetime Income

- Guarantees a baseline level of income (e.g., 5% of a protected account value) that can be taken as withdrawals from the retirement account each year.
- Guarantees that, even if the account is depleted, the insurer will continue sending checks for the guaranteed income amount to the recipient for life (and, in some cases, to a surviving spouse for life).

Preserves a Measure of Liquidity and Control

- Does not require people to turn over their lump sums in exchange for a monthly “paycheck.”
- Investor’s assets must remain invested throughout retirement in one of a menu of well-diversified portfolios.
- Allows the income recipient to stop withdrawals at any time, or to tap into the remaining account balance for unforeseen expenses.

Eliminates the “What if I die too soon?” Concern

- Provides for any remaining account value to be passed along to heirs, even after income payments have commenced.

Prudential’s Four Pillars of Retirement

The Four Pillars of Retirement represent the foundation of retirement security today, from Social Security to the choices made in retirement. Prudential uses these pillars as a framework for research reports, press releases and other information about the retirement issues and challenges facing Americans today.



SOCIAL
SECURITY



EMPLOYMENT-
BASED PLANS



PERSONAL
SAVINGS



RETIREMENT
CHOICES



Prudential



What Is a Variable Annuity?

A variable annuity is a contract between you and an insurance company, whereby the insurer agrees to make periodic payments to you, beginning either immediately or at some future date. You can make a single purchase payment or a series of purchase payments, and there are generally no contribution limits. Variable annuities offer a wide range of professionally managed investment options, guaranteed death benefits, and a variety of payout options including guaranteed income for life.

Plus, any investment gains grow tax-deferred. When you need income, annuities generally offer, without charge, annual access up to 10% of purchase payments. Withdrawals are subject to ordinary income taxes and, if taken prior to age 59½, a 10% federal income tax penalty may apply. Withdrawals exceeding a specified annual amount may be subject to a withdrawal charge, which is assessed for a period of time and generally reduces each year. Withdrawals will reduce the living and death benefits.

The costs vary depending on the annuity and include the cost of: issuing and maintaining the contract, the base death benefit, and investment management expenses. Many variable annuities also offer guaranteed optional living and death benefits that, for an additional fee, can help provide an added measure of security during your lifetime, and for your beneficiaries. All guarantees are based on the claims-paying ability of the issuing company.

Your financial professional can help determine which annuity product, optional benefits, and investment allocation may be suitable for your retirement needs. Please read the prospectus for full details, including all fees and charges.

Investors should consider the variable annuity contract and the underlying portfolios' investment objectives, risks, charges and expenses carefully before investing. This and other important information is contained in the prospectuses, which can be obtained by contacting your financial professional. Please read the prospectuses carefully before investing.

Prudential Financial, its distributors and their respective representatives do not provide tax, accounting, or legal advice. Any tax statements contained herein were not intended or written to be used, and cannot be used, for the purpose of avoiding U.S. federal, state, or local tax penalties. Please consult your own independent advisor as to any tax, accounting, or legal statements made herein.

Tax deferral is already provided by a qualified plan, such as 401(k)s. For an additional fee, the annuity provides a guaranteed death benefit and the ability to receive lifetime income.

Payments of guaranteed principal and income, as well as living and death benefit guarantees, are contingent upon the claims-paying ability of the issuing company. Guarantees do not apply to the investment performance or safety of the underlying subaccounts in the variable annuity. Optional living and death benefits are available for an additional fee and may not be available in all states.

Variable annuities are for retirement purposes and are subject to market fluctuation, investment risk, and possible loss of principal.

Annuity contracts contain exclusions, limitations, reductions of benefits and terms for keeping them in force. Your licensed financial professional can provide you with costs and complete details.

Variable annuities are issued by Pruco Life Insurance Company (in New York, by Pruco Life Insurance Company of New Jersey), Newark, NJ, or by Prudential Annuities Life Assurance Corporation, Shelton, CT, and are distributed by Prudential Annuities Distributors, Inc., Shelton, CT. All are Prudential Financial companies and each is solely responsible for its own financial condition and contractual obligations. Prudential Annuities is a business unit of Prudential Financial. Wachovia Corporation is the majority owner and Prudential Financial, indirectly through subsidiaries, is a minority owner of Wachovia Securities, LLC. Prudential Financial, Prudential and the Rock logo are registered service marks of The Prudential Insurance Company of America and its affiliates.

