What can RILAs do for you?

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Registered index-linked annuities (RILAs) offer market-linked growth with defined downside protection. This report explains how RILAs work, the trade-offs they involve, and how they can fit alongside equities and other retirement vehicles as part of the overall retirement plan.

Key points

- **Registered index-linked annuities (RILAs) provide risk and return potential between full market exposure and income-oriented annuities.** Their returns are linked to a market index, with defined downside risk through buffers or floors and defined upside participation levels that may be subject to limits. RILAs thus offer a structured trade-off between growth potential and risk exposure.
- **Downside protection comes with limitations that matter for planning.** Caps, participation rates, spreads, exclusion of dividends, liquidity constraints, and the need to hold the contract through the full term all affect outcomes. RILAs do not offer full upside participation to stocks, so they should generally not be viewed as a direct substitute for equity exposure.
- **RILAs work best as part of a broader retirement strategy.** They are complementary tools whose effectiveness depends on how they may complement other assets (such as bonds, equities positioned for full upside and dividends, and sources of predictable income like Social Security, pensions, or income annuities) within an investor's overall financial plan.

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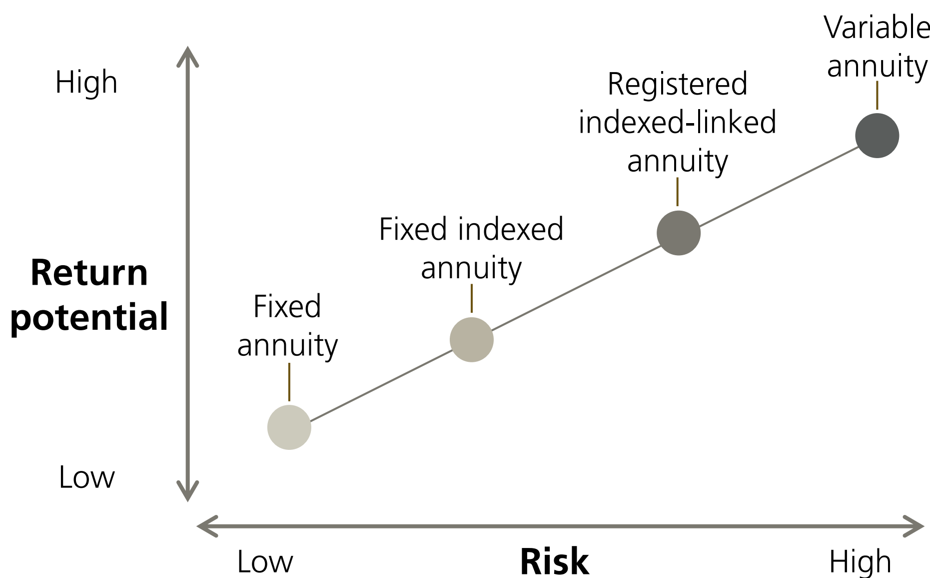
For many investors, annuities are most commonly associated with one primary outcome: providing a steady stream of income. And for good reason: Income-focused annuities can play an important role in helping retirees cover essential spending, manage longevity risk, and reduce reliance on portfolio withdrawals.

However, income is not the only retirement concern that annuities are designed to address. Over time, the annuity landscape has expanded to include solutions that can help manage market volatility and sequence of returns risk. Today's annuity offerings span a wide range of risk and return profiles, with some designed primarily for certainty and income, and others designed to help manage market risk while remaining invested in the markets. At a high level, annuities can be viewed along a spectrum based on how much market risk an investor is willing to accept in exchange for growth potential.

At one end of the spectrum are annuities designed to prioritize certainty and stability, such as fixed annuities. These solutions can provide predictable income regardless of market conditions, but typically require investors to give up liquidity and accept limited long-term growth potential.

Figure 1 - Annuity risk spectrum

Illustrative spectrum highlighting how annuity types vary by market risk and potential return



Source: UBS. For illustration purposes.

At the opposite end of the spectrum are variable annuities, which offer the greatest exposure to market risk (and reward) among annuity types. Variable annuities allow investors to allocate assets to underlying investment subaccounts, so results fluctuate with market performance—generally experiencing the full range of market risk and return potential of underlying asset classes such as stocks and bonds.

Registered index-linked annuities (RILAs) sit closer to the middle of this spectrum, combining market-linked growth potential with defined downside protection. The result is a clearer trade-off between opportunity and risk, usually with returns that follow a formula based on the performance of an underlying index.

When applied thoughtfully within the context of the overall financial plan, RILAs may help investors strike a comfortable balance between growth objectives and risk management in retirement.

What is a Registered index-linked annuity (RILA)?

A RILA is a type of annuity contract that links returns to the performance of a market index, such as the S&P 500, while providing a defined level of downside protection.

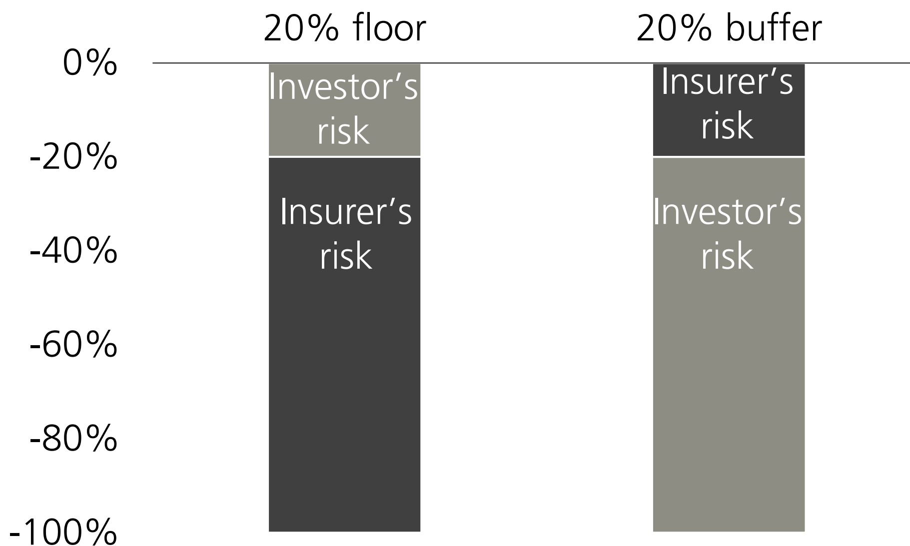
In exchange for limiting potential losses, investors typically accept limits on upside participation. As a result, the risk and return profile of a RILA generally falls between investments with full market exposure and annuities designed primarily for guaranteed income, such as a fixed annuity with a defined rate of return.

How do RILAs work?
RILAs are built around clearly defined outcomes (downside protection and upside limits) over a specified period, usually ranging from one to six years. Returns are linked to the price performance of an underlying market index (the index return excluding dividends) over the course of the term. When the index rises, the investor earns a portion of that gain, subject to contract terms such as caps, participation rates, or spreads. When the index declines, losses may be partially reduced by a buffer or limited by a floor.

At the end of each contract period, gains or losses are automatically locked in. Investors may then choose to exit the contract or allow it to renew into a new outcome period under terms offered at that time.

Key contract features include the following:
- **Buffers** absorb losses up to a stated percentage after which point the investor would incur any excess loss. For example, if the buffer is 10% and the return of the underlying index (e.g., the S&P 500) was -30%, the investor would lose 20%. If the return of the underlying index was -5%, a 10% buffer means the investor's return would be 0%.
- **Floors** limit the maximum loss an investor can experience. For example, if the floor is 10%, the investor won't lose more than 10% regardless of the return of the underlying index.
- **Cap rates** set the maximum index-linked return an investor can earn over the outcome period of the RILA. If the underlying index performs above the cap rate, the investor receives the capped return, not the full index gain. For example, if the RILA has a 12% cap and the index increases by 18% over the outcome period, the investor's return would be 12%.
- **Participation rates** determine how much of the index's gain is credited to the investor, rather than setting a fixed maximum return. For example, if the participation rate is 70% and the index increases by 10%, the investor would earn a 7% return.
- **Spreads** is a percentage that is deducted from the index-linked return over the outcome period. It reduces the return credited in exchange for downside protection.

Figure 2 - RILAs provide downside protection through buffers and floors
Illustrative comparison of buffer and floor protection and how downside risk may be shared

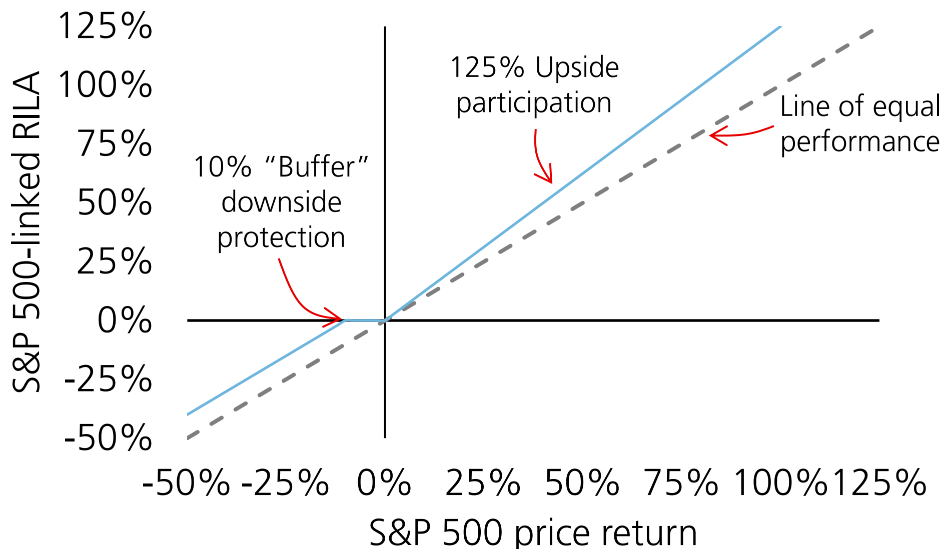


Source: UBS. For illustration purposes.

Example RILA terms
Here is an example of how a RILA may be structured:
- **Index:** S&P 500 Index
- **Term:** Six years
- Upon maturity (e.g., at the end of the six-year period), investors will receive a payment based on the price return of the S&P 500:

- **125% upside participation:** If the S&P 500 is above its starting value at maturity, the investor receives their original investment plus 125% of the index's gain.
- **10% "Buffer" downside protection:** If the S&P 500 is below its starting value at maturity, losses up to 10% are fully protected. If the index is down more than 10%, the investor's loss equals the index's decline minus 10%. *Example: If the index is down 25%, the investor loses 15% (-25% + 10%) and receives 85% of their original investment.*

Figure 3 - RILAs may provide downside protection and enhanced upside participation
Hypothetical return, RILA (y-acis) and S&P 500 Index (x-axis), using example RILA terms



Source: UBS. For illustration purposes.

How are RILAs taxed?
The tax treatment of RILAs depends primarily on whether it is funded with taxable assets or qualified (tax-deferred) assets.

When funded with **taxable (after-tax) assets**, earnings inside the contract grow on a tax-deferred basis, allowing returns to compound without annual taxation. Upon withdrawal, only the earnings portion of each distribution is taxed as ordinary income while the return of principal is not taxed. Withdrawals are generally taxed on a last-in, first-out basis, meaning earnings are taxed before principal. Withdrawals taken prior to age 59½ may also be subject to a 10% early withdrawal penalty.

For investors who would otherwise hold assets that generate recurring taxable income or realized capital gains, tax deferral can be valuable, particularly over longer holding periods. However, this benefit should be weighed against the fact that RILA earnings are ultimately taxed at ordinary income rates rather than at potentially lower long-term capital gains rates.

When a RILA is funded with **qualified (tax-deferred) assets**, such as a Traditional IRA or 401(k), the assets maintain their tax-deferred status, meaning distributions are taxed as ordinary income regardless of the investments used.[1]

As a result, deciding how to fund a RILA is less about identifying a universally superior tax outcome and more about aligning the contract's role with the investor's overall retirement strategy, liquidity needs, time horizon, and tax situation.

Understanding the trade-offs and risks

RILAs are designed to help investors balance two competing retirement objectives: staying invested for growth while limiting exposure to large market declines. Understanding the trade-offs involved can help clarify whether a RILA is appropriate for a given planning objective.

- **Downside protection comes with limited upside**: RILAs (Registered Index-Linked Annuities) may offer downside protection through features such as buffers (which absorb a set percentage of losses) or floors (which set a maximum loss, such as -10%). Having defined, and more predictable outcomes may help some investors stay invested during

volatile periods. In exchange for these characteristics, RILAs generally have limited potential for gains, and their returns may lag direct market exposure. Here are some examples of ways that upside potential may be limited:

- **Caps:** The maximum return that the investor can earn in a period, even if the index rises more.
- **Participation rates:** The percentage of the index's gain that is credited to the investor's account (e.g., if the index rises 10% and the participation rate is 80%, the investor receives 8%).
- **Spreads:** A set percentage subtracted from the index's gain before the investor's return is calculated (e.g., if the index rises 10% and the spread is 2%, the investor receives 8%).
- **Foregone dividends:** RILA returns are typically based on the price return of an index (e.g., excluding the index's dividends) when calculating the investor's credited returns.

- **A 0% floor does not eliminate market risk**: A 0% floor means that the investor cannot lose money due to index declines if they hold the contract to the end of its term. However, this does not make the investment risk-free. Other risks remain, such as missing out on higher returns elsewhere (opportunity cost), limited access to the invested assets (liquidity constraints), and less flexibility to change the investment strategy during the RILA's term.
- **Outcomes depend on holding through the full term**: Interim values can fluctuate with market conditions and early withdrawals may reflect market declines and surrender charges.
- **Liquidity is limited**: Most RILAs include surrender charge schedules and limits on withdrawals during the surrender period, making them generally unsuitable for assets needed for near-term spending.
- **Insurance company credit risk applies**: RILA payouts are backed by the issuing insurer's claims-paying ability. This means that if the insurer were unable to meet its obligations, the guarantees provided by the RILA could be at risk. Generally, highly rated insurers are considered to have strong creditworthiness and often maintain higher capital reserves than banks. However, RILAs are generally not protected by government insurance (such as FDIC or SIPC), so investors should carefully consider the credit quality of the issuer before investing.[2]

When used thoughtfully and aligned with an investor's goals and time horizon, RILAs can help manage market risk, but only by accepting limits on upside, liquidity, and flexibility.

Who may benefit from a RILA (and who may not)?
RILAs may be appropriate for investors who are concerned about market volatility near or in retirement but still want continued exposure to equity-like growth with defined risk limits. Since they involve some market risk and might not provide income during the contract period, they are best suited for investors with longer time horizons and limited near-term liquidity needs.

By contrast, investors seeking full liquidity, short holding periods, or highly flexible portfolios may find other investment approaches more appropriate. RILAs may also be less suitable for investors with very low risk tolerance or those who require guaranteed returns, or immediate or guaranteed income where traditional income annuities or more conservative strategies may be a better fit.

How to think about RILAs in the context of a retirement plan

RILAs can be structured in many different ways, and small adjustments in design can lead to significantly different outcomes. A useful way to evaluate a RILA is to start with the question, "What problem is the investor trying to solve?," and then use the contract terms to confirm whether the structure aligns with that objective.

1. Start with the concern. Before focusing on caps, participation rates, or buffers, it is important to clarify any concerns the investor is looking to address. RILAs are most often used to help manage market risk and reduce the emotional and financial impact of market declines. Potential roles for RILAs in a retirement plan include volatility management, behavioral support during downturns, and planning around the years when sequence risk may be most significant. If the primary goal is near-term liquidity or immediate cash flow, a RILA is unlikely to be the right tool for the task.

2. Set expectations for returns. Most RILAs' returns are credited using the price returns of the underlying index, excluding dividends. As a result, participation rates that appear attractive in isolation may translate to different outcomes depending on the market scenario and underlying index.

With this in mind, there are two relationships to note:
i. Higher dividend yields increase the upside participation required for a RILA's return to match total return.
ii. For a given dividend yield, lower price returns require higher participation because dividends represent a larger share of total return when price returns are low.

Figure 4 - How much upside participation may be needed to keep pace with total return?
Illustrative 1-year heatmap of the implied participation rate needed to match index total return (price + dividends)

Dividend yield \ Index price return	2%	4%	6%	8%
1%	150%	125%	117%	113%
2%	200%	150%	133%	125%
3%	250%	175%	150%	138%

Source: UBS. For illustration purposes. Note: A binding cap or spread may limit credited returns and affect the ability to match total return.

This does not mean that a RILA must outperform total return in order to be effective. Some investors may consider RILAs because they are willing to accept limited upside participation in exchange for defined downside protection. Other investors may use RILAs for bond replacement and may be unconcerned with directly outperforming stocks. Even still, understanding the dividend, return, and participation dynamic helps establish realistic expectations.

3. Match downside protection to how much risk the investor is willing (and able) to accept. Downside protection characteristics will tend to be triggered more often for RILAs with a shorter time horizon because market losses are more common over shorter time frames than long time frames. For example, according to Bloomberg data looking at rolling returns since December 1945, the S&P 500 Index has registered losses in 21% of 1-year periods, 10% of 3-year periods, and 2% of 6-year periods. For longer-term RILAs, gains are more likely to be common, so opportunity cost may be a more potent "risk" for the investor, in which case upside leverage may be a greater priority than downside protection.

4. Align the RILA's duration with the purpose of those assets. RILAs are designed around defined time periods (one, two, three, and six years), and the stated upside and downside terms generally apply at the end of that period. What's more, most RILAs include limits on withdrawals during the surrender period and may also include surrender charges. For these reasons, the most practical way to think about duration decisions is to align it with the assets' purpose and the investor's ability to remain invested through the full RILA term.

Shorter periods (e.g., one year) may be preferable when flexibility matters most. They create more frequent "resets," allowing investors to reassess terms and reposition capital more often. But, they can also make outcomes more sensitive to the return environment in any single year.

Longer outcome periods (e.g., three to six years) provide more time for market outcomes to unfold, but liquidity planning remains important across all RILA terms, as surrender periods generally extend beyond a single outcome period and typically do not vary based on whether the index term is one year or longer.

5. Consider funding source and portfolio integration together. A RILA is not designed to be a complete retirement solution on its own. Instead, it is a partial tool intended to address a specific objective, most often managing market risk for a portion of the retirement assets. For this reason, decisions about how to use a RILA are best made in the context of the overall financial plan and investment strategy, rather than by evaluating the contract in isolation.

Because most RILAs limit upside and typically exclude dividends, they tend to work best alongside other assets that are designed for different roles. These may include bonds designed to provide income and principal protection; equities positioned to capture full market growth and dividends; and as sources of predicable income such as Social Security, pensions, or income annuities. In this case, the RILA is not expected to do all the work; instead, it's expected to help manage risks while other portfolio components help support growth and income.

When deciding whether to fund a Registered Index-Linked Annuity (RILA) allocation from stocks or from bonds, investors may want to consider whether the RILA is intended to act as a stock substitute, a bond substitute, or a "hybrid" allocation. Here are some factors that investors may want to evaluate:

- RILAs typically offer partial downside protection and capped upside, so reallocating from stocks may reduce overall portfolio risk and volatility, potentially smoothing returns during market downturns in exchange for limited growth participation. For RILAs with returns that are correlated to their underlying index, shifting assets from stocks to RILAs may not offer a diversification benefit. Some RILAs do offer uncorrelated returns, and may therefore enhance portfolio diversification as a complement to a stock allocation.
- RILAs generally have higher risk and return potential than traditional bonds, because their returns are typically linked to equity market indexes. RILA returns are typically uncorrelated to bond market returns. Reallocating from bonds to RILAs may enhance portfolio return potential, at the expense of reduced diversification. Funding from bonds increases portfolio risk and equity exposure, which may not be suitable for conservative investors or those seeking stable income.

The success of a RILA typically depends less on its individual terms and more on how well it complements the rest of the portfolio. When integrated thoughtfully—accounting for time horizon, liquidity needs, tax considerations, and existing income sources—a RILA may help balance opportunity and risk as part of a comprehensive retirement strategy, rather than functioning as a standalone solution.

Related consideration: Structured investments

Some investors may also explore structured products, which share similarities with RILAs. Like RILAs, structured products offer defined return profiles tied to market indexes, often combining partial downside protection with limits on upside participation over a set term.

Unlike RILAs, structured products are typically issued as securities rather than insurance contracts, meaning they do not offer tax-deferral or insurance guarantees and may carry different risks, costs, and liquidity features. In certain circumstances, and depending on an investor's objectives, tax situation, and tolerance for issuer credit risk, structured products may warrant consideration alongside RILAs as part of a broader discussion about managing risk and return in retirement planning.

If you'd like to learn more about structured investments, please see the CIO Research team's educational reports on the subject, including the following:

- Structured Investments: Considering outcome-oriented investments, published 7 December 2023
- Structured investments: Strategies for three investor challenges, published 5 June 2024
- Structured investments 101: Risk, return, and positioning considerations, published 31 July 2025

End notes

[1] RILAs purchased with qualified assets are subject to required minimum distributions (RMDs). RMDs are generally calculated using the contract's value as of 31 December of the prior year. If the annuity includes additional benefits or riders, the value used to calculate RMDs may differ. Investors should consult their form for guidance on how their specific RILA is treated for RMD purposes.

[2] US Securities and Exchange Commission. Annuities. Investor.gov. Retrieved March 30, 2026, from https://www.investor.gov/introduction-investing/investing-basics/investment-products/annuities.

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