

Risk is Opportunity.™

Retirement: Risk is Opportunity Closing Session (Session 66)

Ron Gebhardtsbauer
Dawn Helwig
Dale Yamamoto
& Emily Kessler (moderator)



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Actuaries
Risk is Opportunity.™

What do you think?



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Retirement: Risk is Opportunity

- Looked at the risks and opportunities in retirement
 - Pensions/Income
 - Health Care
 - Long-Term Care



Retirement: Risk is Opportunity

- Opening Session outlined the issues
- Breakout sessions dived deeper into the risk and considered specific solutions or new ideas for each specific risk (income, health, long-term care)
- Closing Session: what you think of various possibilities



Red/Yellow/Green

- Panelists will present specific proposals
- You Vote
 - Use red/yellow/ green cards
 - ◆ **Green:** Like it
 - ◆ **Yellow:** Not sure
 - ◆ **Red:** Hate it
 - One rule: may only hold up one card at a time
- Discussion: why people liked it, hated lit or weren't sure



Pensions

Ron Gebhardtsbauer
Senior Pension Fellow
American Academy of Actuaries

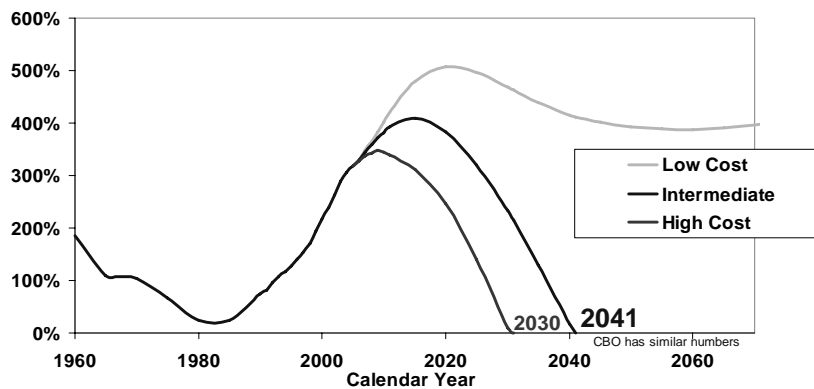


Pensions

- All 3 legs have problems:
 - Social Security has financial problems
 - Many employers abandoning DB
 - ♦ 401(k)s often not adequate
 - Individual Savings - low
- Social Security surpluses not saved
 - Baby boomer entitlements huge



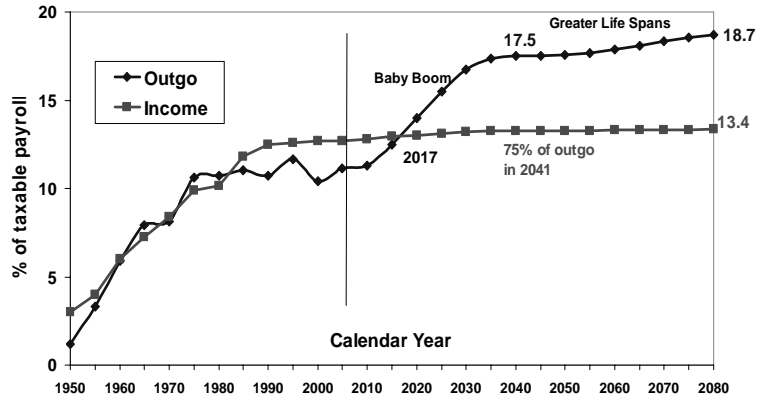
Social Security Trust Fund Ratios
(Beginning of Year Assets as a Percentage of Expenditures)



The Trust Funds are projected to be exhausted in 2041 using the Intermediate Assumptions. The assumptions are reasonable in the aggregate per GAO/PWC report & individually reasonable per SS Chief Actuary. On low cost assumptions, Social Security could be solvent & sustainable (trust fund ratios stable or increasing around 75th year) but is unlikely to happen (< 5%). 2007 Trustees Report Tables IV.B3 & VI.A4.



Social Security Income & Outgo
Intermediate Assumptions

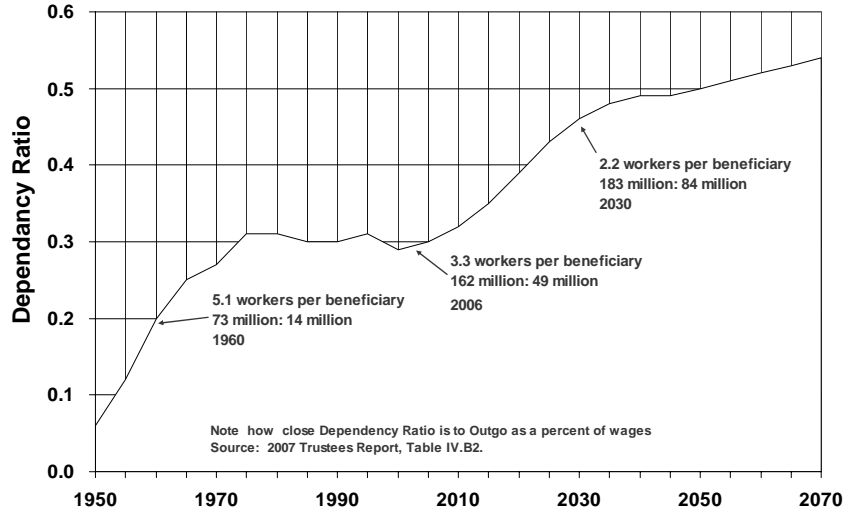


2007 Report Table IV.B1. Using low (high) cost assumptions, the 2085 outgo is 13.4% (27%), and the 2017 date is 2022 (2014). The unfunded obligations over the next 75 years = \$5.1 trillion = -1.95%, -5.05 & 0.36% of taxable payroll for the intermediate, high, & low cost assumptions, per Table IV.B4. 70% of outgo in 2081 per Fig. II.D2



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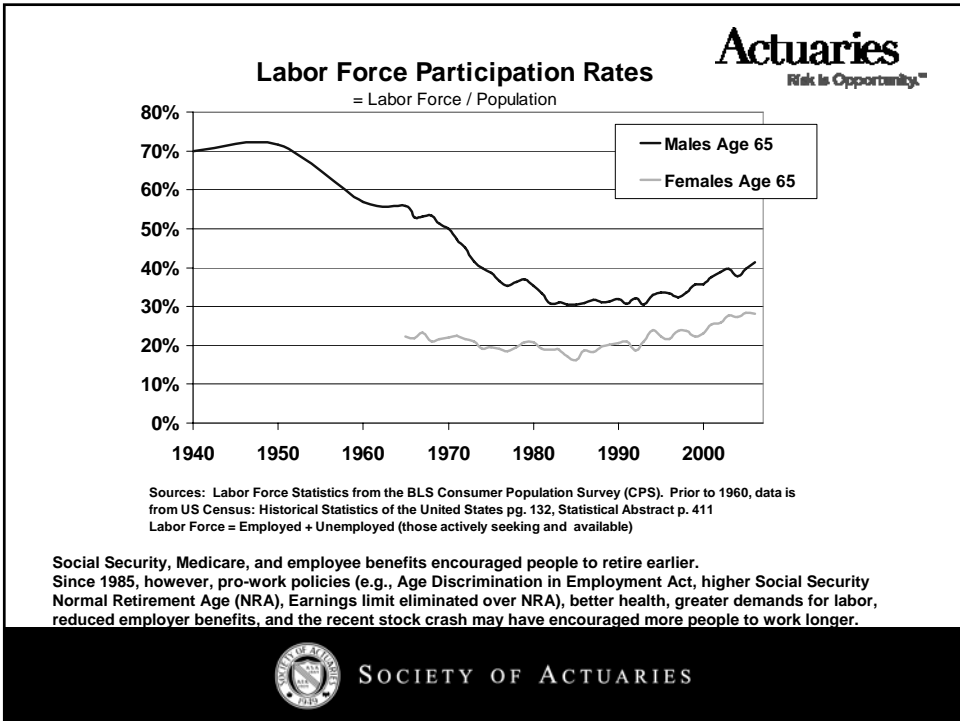
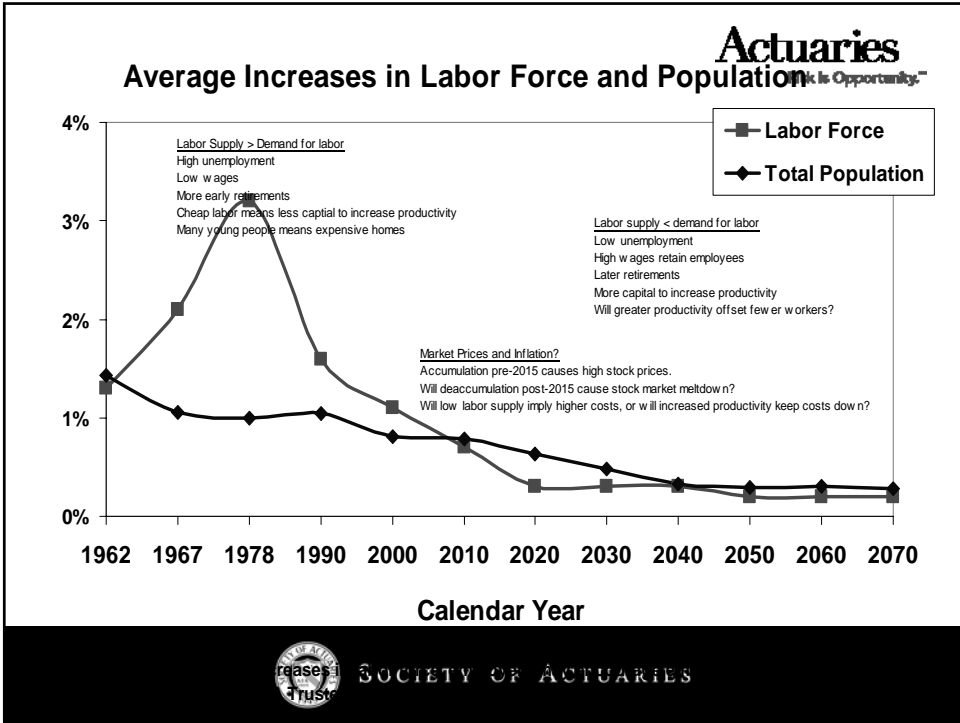
Dependency Ratio = Beneficiaries per Covered Worker



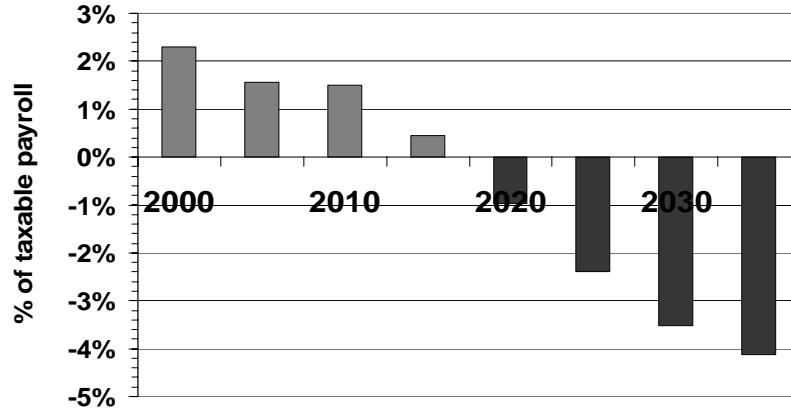
Note how close Dependency Ratio is to Outgo as a percent of wages
Source: 2007 Trustees Report, Table IV.B2.



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**Social Security Net Cash Flow
(Contributions - Benefits)**

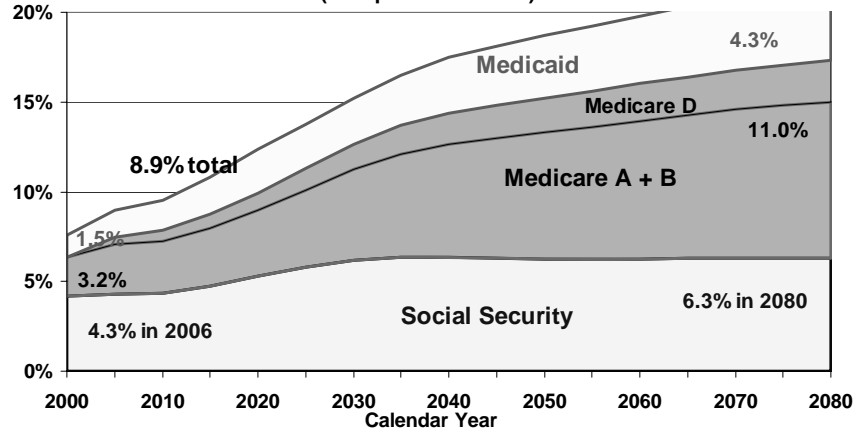


2004 SS Trustees Report Table IV.B1
Net Cash Flow will go negative around 2018 (intermediate assumptions).
The 75 yr actuarial balance = -1.87% of payroll.



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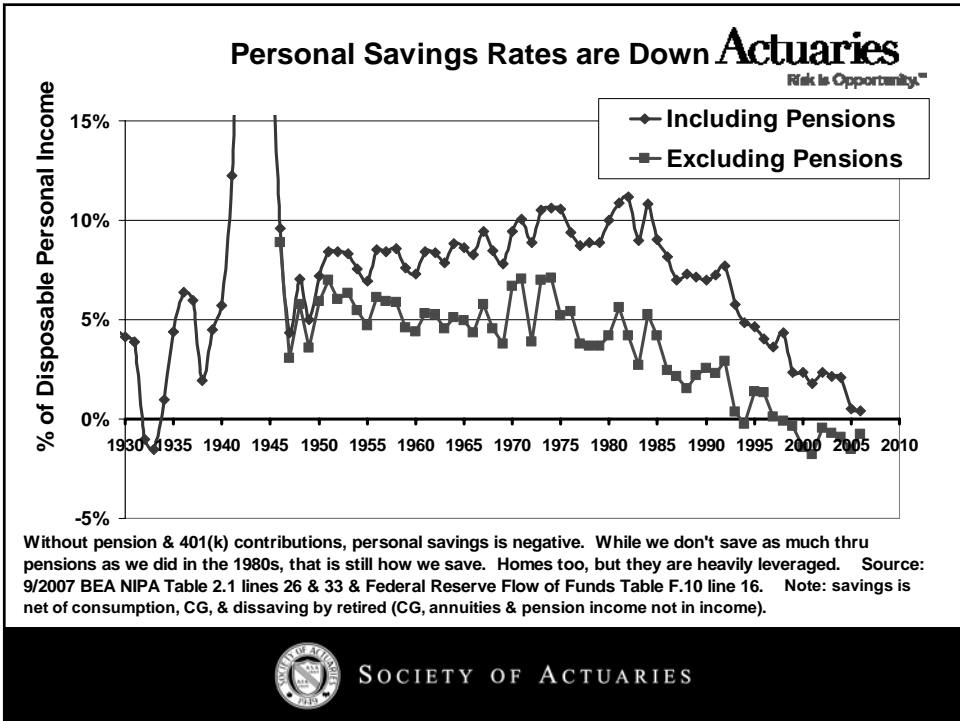
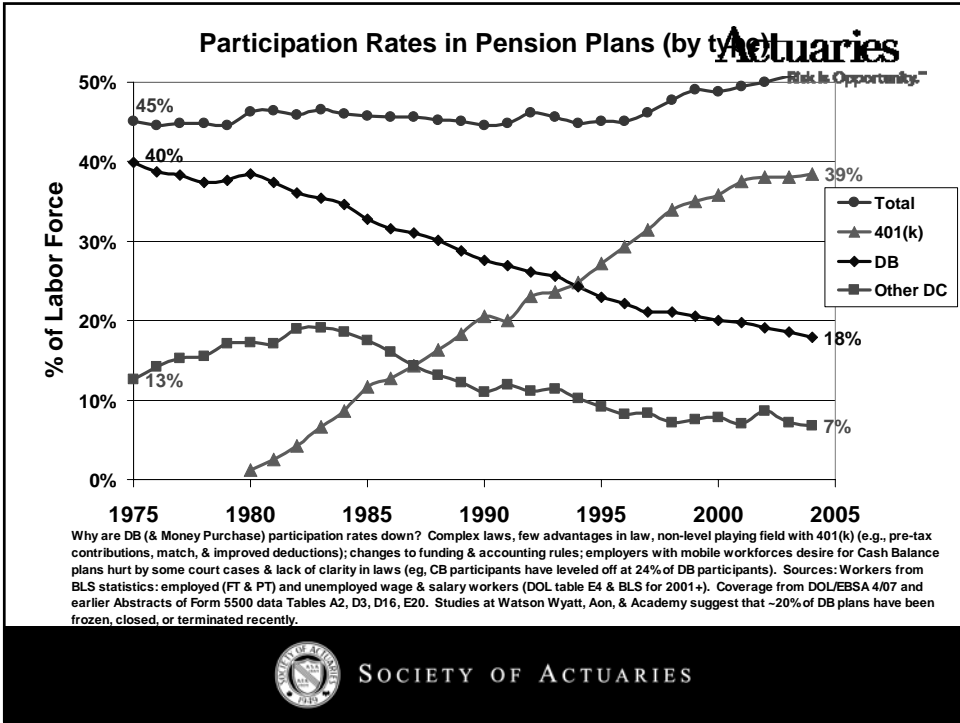
**Total Costs of Social Security, Medicare, & Medicaid
(as a percent of GDP)**



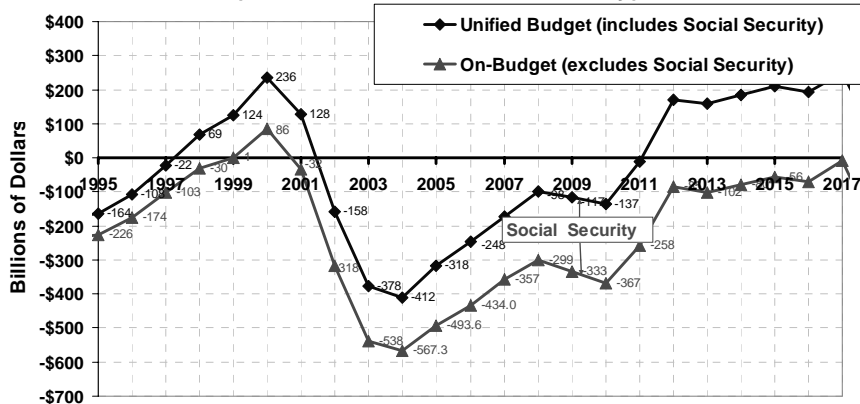
Sources: 2006 OASDHI Table VI.F4; SMI (Parts B & D) from Medicare report Tables III.C14 & 20; & Medicaid projected from CBO 12/2005 Long Term Budget Outlook. Today, these programs are half of non-interest government expenses. Total costs more than double to 21.6% by 2080 (Medicare more than triple, surpassing SS by 2028 per Conclusion on p. 27) and eventually exceed 20% of the economy, which would require taxes to increase or government programs shrink.



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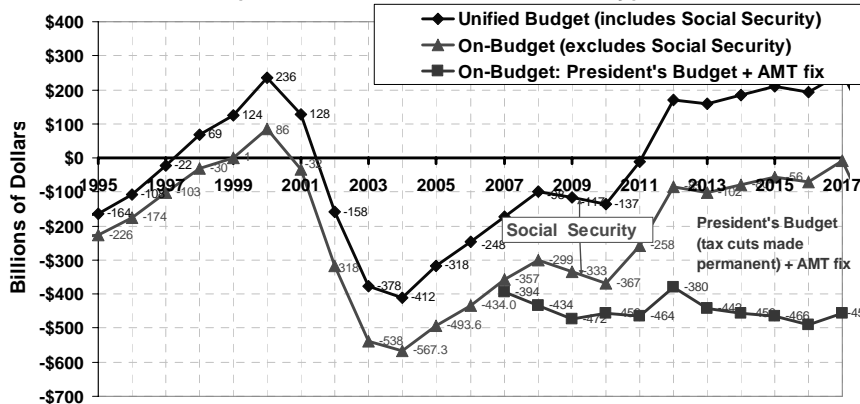
**Federal Budget Surplus
(with and without Social Security)**



Source: 1/2007 CBO Budget Outlook & 3/07 Analysis of President's Budget. "Deficits don't matter" today (they stimulate economy), but they matter to our kids who have to pay for them. On budget deficits will continue if tax cuts made permanent, AMT fixed, health costs increase faster than GDP, Iraq War continues, SS Individual Accounts enacted, etc. Deficits get much larger again after 2017 per CBO 6/2002 long range fiscal policy brief. Note: Off-budget agencies also include USPS, but minor.



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Idea #1 – Save Social Security

- Fix Social Security's financial status For example:
 - Raise NRA gradually (1 month/2 years)
 - Tax SS benefits like pensions (reduces complexity & inequity)
 - Make truly universal: bring in remaining States
 - Increase # of years in wage average (retirement age neutral)
 - Reduce/eliminate "free" spouse benefit & replace with wage sharing
 - Keep progressive benefit formula & inflation-indexed annuity
 - Invest above gains in market & eliminate deficit (not to cut FIT)
 - Fix without FICA tax increase? (Medicare & Add On IA will need it)

Red: high vote getters from 20/20 conference. Black: not an Academy idea; just a list



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Idea #2 – Increase Savings for All

- Mandate Add-On Individual Retirement Account (1% Er & 1% Ee) Social Security not enough
 - Mandates are cheap – they don't require tax incentives
 - Employers just send a larger FICA/FIT check to government
 - ◆ Invest like Federal TSP until large enough for individual to take over
 - Mandatory Annuitization (up to say 1 ½ x poverty level)
 - Allow waiver if provided thru employer or other group or IRA or insurer



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Idea #2 – Increase Savings for All

- Encourage additional personal savings
 - Continue §25B Saver's tax credits for low income in DC and IRAs
 - Extend to Cash Balance (& other DB?) plans; make non-refundable
 - Tax expenditure low because distribution taxed & reduces Medicaid
 - Ensure financial advisors to act honestly/benefit of consumer
 - Standardize products (e.g., longevity insurance) so it's easier to shop/compare
- Tax policy should smooth govt. costs across generations
 - Pension plans move today's taxes to future when it is needed more
 - Less Roth ideas until big deficits return



Idea #3 – Encourage Groups/Pooling

- Encourage Group provision (Employer DBs, Netherlands, Multi's, Associations, etc.)
 - More efficient/more people. Pooling doesn't work well in DC plans
 - Encourage Employer DBs
 - Encourage hedging products – longer bonds & zeros retail direct from Treasury
 - Fix Reversion tax - Sponsor get upside of good investment returns
 - Why do Cash Balance rules require interest credit promise to NRA?
 - Level playing field or Return to larger incentives for DB
 - Make DC more like DB. Auto-enroll; Auto-Annuity; Auto-Actuary
 - Employer helps get annuity
 - 401(k)s - require minimum contributions from DOH
 - Require longevity insurance with lump sum
 - 401(k) fees should be fully disclosed; Commissions should align agent with participants



Idea #3 – Encourage Groups/Pooling

- Encourage employers/groups to educate/provide experts (cheaper in groups)
 - Change motivation; expert's compensation shouldn't influence advice
 - ◆ Even fee-only financial advisor biased against annuities
 - Educate workers on advantages of annuitizing; saving more
 - Assist in annuitizing through group mechanisms
- Encourage annuitization with tax advantages
 - Tax free up to certain level, even in DB plans



Idea #4 – Encourage Later Retirement

- Raise what we think is “Normal” RA
 - ◆ Raise Social Security's NRA
 - ◆ Increase # of years in average wage calculation
 - ◆ Continue Social Security's actuarial increases to 75
 - ◆ Raise Eligibility Age for Medicare too
 - ◆ Increase minimum distribution age 70 ½ to 75 or 80
 - ◆ Allow later NRA for pensions (or tie to SSNRA)
 - ◆ Allow deferred pensions at age 85 with 401(k)
- Simplify/encourage phased retirement
- Require 401(k) benefit statements to show annuity amount



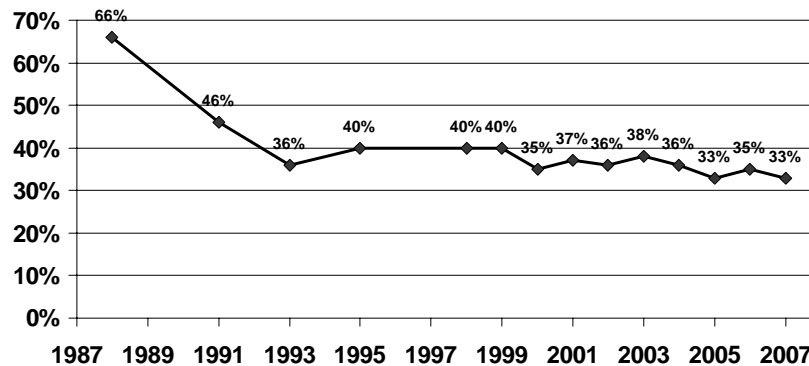
Health Care

Dale Yamamoto
Hewitt Associates



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Prevalence of Retiree Medical

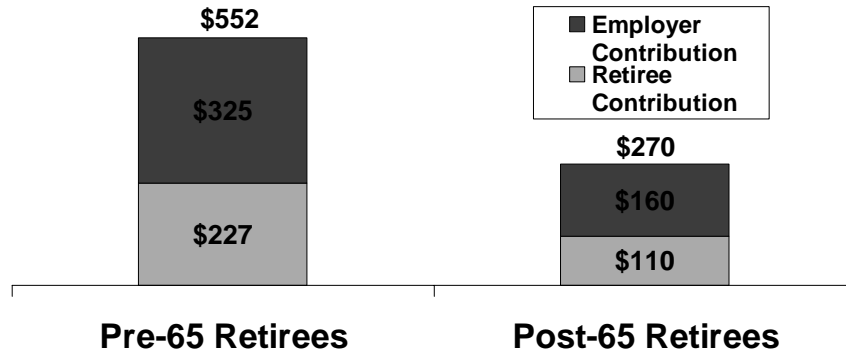


Source: Kaiser/HRET survey of employer-sponsored health benefits. Percentage of large firms (200+ employees) offering health insurance to retirees



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2006 Average Monthly Premiums

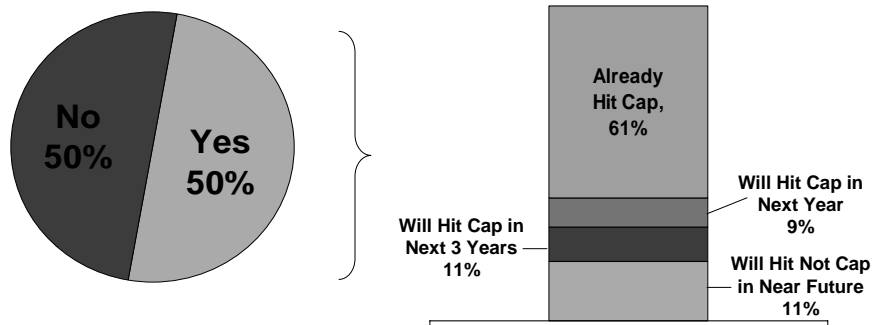


Source: Kaiser/Hewitt 2006 Survey on Retiree Health Benefits, December 2006



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Employer Caps

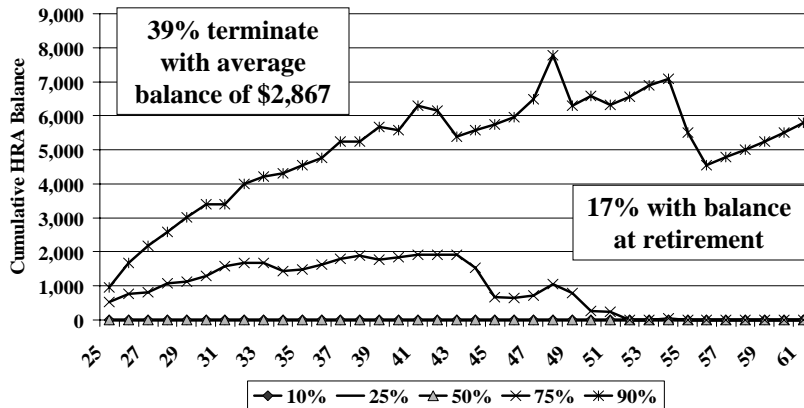


Source: Kaiser/Hewitt 2006 Survey on Retiree Health Benefits, December 2006



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Small % with Balance

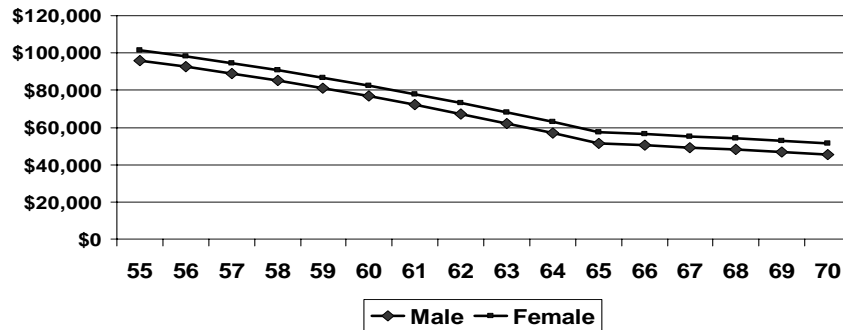


Note: \$1,000/year, indexed 5%, claims trended 8%, 6.5% interest



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PV of Medical in 2006



Key assumptions: 8% discount rate, 9% grading to 5% in 9 years healthcare trend, RP 2000 healthy mortality, KFF/Hewitt 2006 average costs



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Health Care Idea #1

- No change in health care delivery
- Increase communication efforts
 - Upfront communication of expected costs
 - Provide modeling tools
 - Enhance healthcare provider information on efficiency and effectiveness



Health Care Idea #2

- Further enhance health savings accounts
- Allow accounts without ties to high deductible health plans
- Increase maximums (both under and over age 50)



Health Care Idea #3

- Introduce government-run catastrophic program (universal)
- Require basic employer-sponsored coverage (active employees)
- Require individual coverage (non-employees)
- Eliminate rich Medigap plans



Long-Term Care

Dawn E. Helwig, F.S.A., M.A.A.A.

Milliman, Inc.

71 S. Wacker Drive, 31st Floor

Chicago, IL 60606

(312) 726-0677

dawn.helwig@milliman.com



LTC Idea #1: Medicaid Reform

- State enforcement of 2005 Deficit Reduction Act initiatives
- In addition: require home value to be included in assets used to qualify a person for Medicaid, thereby eliminating Medicaid's long term, free "loan" on home value
- Enhance "Grannie Mae" type private programs, to allow loan of full value of home (reverse mortgages)
- Save Medicaid for the truly indigent



LTC Idea #2 – Short term LTC Supplemented by Catastrophic Medicaid

- Mandate purchase of short term (3 years?) LTC policy, provided by insurers or through reverse mortgages
- Government provides care for care beyond 3 years, through tax-financed program (universal coverage)
- Medicaid continues to pay for all coverage for indigent (with housing included in means testing)



LTC Idea #3 – Medicare Part E

- Combined current Medicare LTC coverage with Medicaid coverage into Medicare Part E
- Enrolling in Part E would be mandatory (with Medicaid available for truly indigent)
- Coverage would have deductibles and copays, which would be funded through private Medicare Part E supplemental policies
- Increase in payroll taxes needed to fund



LTC Idea #4 – Pretty Much “Business as Usual”

- Continue Partnership initiatives
- Pass tax incentives for private LTC purchases (above the line tax deduction and 401(k) style plans to pay for LTC)

