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Comments on

"The Total Career Benchmark Model: A Pension Model for *Retirement 20/20*"

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1. Overview

This paper is comprehensive, creative, and well-developed, proposing a mandatory retirement system that is fully integrated with and linked to the Tier I social insurance system. While the design is complex, it results in mandatory coverage that systemizes all participants into a "unit scale" based on average wages resulting in predictable and adequate base benefits as well as the ability to fund supplemental retirement income. The complexity may be mitigated somewhat by the universality of coverage and the communication aspects envisioned through the centralized administration. In addition, the design establishes targets and communicates how close individuals are to reaching those targets so they can easily see how to fill the gaps. There is a good integration with Tier I social insurance, which helps people see the value of that piece and what they have to make up through their personal savings. In addition, the Personal Accounts give individuals some discretion to plan for additional voluntary retirement savings based on their own particular needs. The plan removes the employer from being the primary "insurer" of both investment and longevity risk, while also providing some design flexibility that allows the employer to vary contribution levels to meet business needs. In fact, it is the employer's role that changes the most from the current structure to this model. While written for a Canadian context, the ideas are generally translatable to the United States.

2. Key Elements of the System

The Lifetime Account, which includes all employer and required employee contributions, provides for a guaranteed annuitized life income through mandatory contributions on income up to Average Industrial Wage ($47,800 for 2011) to ensure a minimum level of savings. Personal Accounts can also be established to provide individual flexibility, fund personal risks, and provide ancillary benefits such as early retirement, spousal benefits, cost-of-living greater than Average Industrial Wage increases, post-retirement medical costs, and part-time work. It provides full portability and minimizes leakage, with the possibility to transfer funds between accounts, and also ensures universal access for all types of employment.

The system provides for the ability to centralize and integrate the tracking of the overall retirement savings (Tiers I and II), while facilitating communication with individuals and enhancing their understanding of retirement goals by providing standardized information with continuous benchmarking. The employer still plays an educational role, but the administration burden is streamlined and reduced.

While the employer is a contributor and "champion," not an insurer or guarantor, the plan can still be designed to align with the employer's needs, goals, risk tolerance, and financial situation. Most risks are mitigated through pooling of longevity risk, automatic tracking of pre- and post-retirement inflation and ensuring a minimum amount of annuitization prior to or upon retirement. Markets and investment expertise are utilized through Approved Annuitization Funds (AAFs) and Age-Specific Plans (ASPs), which can include insurers, banks, or large pension plans. Transition from the current system through evolution over the next 15 years is also addressed.

3. Pros

- By integrating the three pillars of retirement savings and centralization, the system facilitates communication and understanding of objectives and builds social solidarity by helping individuals see the value of the social insurance and what they have to make up on their own.

- It provides individuals with universal access to professional investment expertise and guaranteed income.

- Mandatory employee contributions should increase employees' engagement in and appreciation of their retirement benefits.

- The use of Lifetime and Personal accounts helps adjust to changing conditions and minimizes demographic risk.

- Targets are designed to ensure adequacy combined with strong communications to keep individuals on track.

- The employer is not in the benefit guarantee business but does play an educational role and can continue to be a "trusted advisor" to employees.

- Benefit design is predictable through ties to external indices.

- Longevity risk is pooled, which should lower the cost of annuitization.

- Indexing to average wages includes pre-retirement inflation protection.

- It includes a universal access tool and transparent structure to ease understanding of accumulated retirement savings versus objectives.

- Design flexibility can align with employer workforce needs.

- Benefit levels can be easily tailored, which should make it easier to "compete" because all plans are comparable.

- Contributions can be increased (somewhat) to encourage early retirement.

- It is responsive to owners since contributions can also be decreased.

- It gets the employer out of the business of sponsoring plans, which is especially attractive to small employers.

- It can be operated to use the markets extensively and efficiently while allocating risk properly.

- It can be designed to have strong governance, and the similarity of plan structures should allow easy scrutiny.

- Roles are set to maximize individuals' strengths and use behavioral finance theories effectively.

- The use of career limits improves fairness in the system.
- It can be structured to hedge risks.
- Costs are minimized due to the size of the system.
- Having everyone in one centralized system and linking it to social insurance should ease administration.
- While it is relatively complex, it does systemize all participants into a "unit scale" based on Yearly Maximum Pensionable Earnings (YMPE; average wages).
- It gets small employers and self-employed individuals into the pension system on a tax- and benefit-equalized basis. In addition, groups such as unions can be plan sponsors.
- Built-in limits for tax-deductible contributions are a good level to ensure adequacy of income.
- Extensive communications and online access are generally provided by large employers now, but this model would make them available to all employees.
- The focus is on savings and not on investing.
- Accumulation of wealth is expressed in terms of income and not a lump-sum dollar amount.

4. Cons

- It does not fully address sustainability across generations.
- There is a concern about system failure in event of market meltdown or extreme events (depending on structure of ASPs).
- It does not address different retirement savings needs depending on income level.
- It appears to be a very complex system to set up and for individuals to understand initially with a steep learning curve.
- Individuals still need to make decisions to convert credits into Lifetime Account and manage their Personal Accounts.
- It may lead to employers having less control over design and workforce management.
- Tying retirement age to the Tier I definition may send a signal about what the "normal" retirement age is.
- Risk bearing may not be obvious to individuals due to the complexity of the system.
- It is not fully clear who bears investment risk.

- The use of market mechanisms is not transparent.

- It is not obvious how the transition from current plans would work.

- The proposal feels onerous (e.g., having to recalculate the available tax deductions).

- The addition of more autopilot features (e.g., automatically recommending a personal contribution for next year to keep employees on track or providing set packages of personal benefits) may be desirable.

- It may not be practical or cost-efficient to figure out everyone's accumulated tax limit at transition.

5. Questions for the Author

- Who chooses the AAFs and how are they monitored?

- Is the employer a fiduciary?

- What happens if ASP operators take too much risk?

- What happens if ASP operators generate additional profits?

- What do AAFs trading ASP units do to help them; e.g., if it is a group annuity, how can that be given to another insurer, and shouldn't it have the same value for one AAF as another? Can they be hedged like insurers?

- If an AAF manages an ASP, are there conflicts of interest?

- Is it clear who bears what risks? If not, how can this be addressed?

- What happens if there are significant cohort longevity gains?

- How would the universal national mandatory provision "play" in the United States, especially in light of the ongoing debate over mandatory health care and the fact that businesses and employees generally do not like mandates and there is increasing concern over government control?

- Can employers tailor retirement ages to meet specific needs (e.g., public safety employees or those in physically demanding jobs who have a shorter working lifetime)?

- Can employers offer ad hoc early retirement "windows"?

- Can the markets hedge the YMPE indexation?

- Will individuals understand how to manage their Personal Accounts?

- Will all employees have access to the online tools that are necessary for understanding and managing their accounts?

- How will the transition from existing plans work?
- Will the transition be too difficult if we have to "reboot" the systems?
- Who pays the fees?
- If we build it, will they come; i.e., will the markets step up and create the innovative products needed in a timely manner, especially for disability benefits?

6. Conclusion

The Total Career Benchmark (TCB) model effectively solves the problems of coverage, portability, income adequacy, and income security in the current retirement system through nationalization, standardization, centralization, mandates on contributions, and annuitizations. It highlights the need to make financial education and literacy a top priority. It includes elements of shared responsibility and transparency but doesn't lose sight of the importance of the employer role. It is generally a well-thought-out proposal, and the pros greatly outweigh the cons. It contains viable components that effectively incorporate *Retirement 20/20* principles and can be used to advance the discussion of a national retirement income policy in both the United States and Canada.

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