



Article from

In the Public Interest

January 2016

Issue 12

Individual Equity and Social Adequacy

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An important part of actuaries' education and training is the instilling of respect for two important principles: individual equity and funding of future contingent payments. Individual equity means that each insured individual's premiums or contributions are based on the actuarial present value of that same individual's future benefits (in other words, on that individual's risk characteristics). Funding means that promised contingent payments are secured by assets held by the insurer or pension fund for that specific purpose.

These two principles have a clear purpose in private insurance and pensions, where participation is voluntary, and entities that promise benefits may weaken or cease to exist due to market forces. If premiums charged by a private insurer are not closely related to each policyholder's risks, and some policyholders are subsidizing other policyholders, another insurer can profitably offer a better deal to the overcharged policyholder, leaving the first insurer mainly with the undercharged policyholders, whose premiums do not adequately cover their expected benefits. If a company that promised pensions to its workers goes under without sufficient assets to pay those pensions, the workers will never receive part of their promised compensation and will likely experience financial hardship in old age.

In social insurance, however, individual equity and funding are often not necessary, and sometimes may not even be desirable. If

participation in an insurance program is mandatory and universal, adverse selection becomes irrelevant, and it is feasible to set contributions and benefits to achieve a different goal, social adequacy. Also, the sponsoring entity (the state) is not at the mercy of the market: it has taxing power and will not cease to exist. (If it does, we'll likely have worse problems than unpaid benefits.)

The contrast is not always so sharp. Some degree of individual equity in social insurance is usually necessary for the programs to maintain broad political support, and funding may be necessary for programs provided by subnational entities or by countries with less stable governments. Neither are the two principles sacrosanct in the private sector; for example, it is difficult to determine the individual incidence of employee benefit costs, and retiree medical benefits are often not funded.

Actuaries working for government programs and those working in the private sector often have differing perspectives on the role of these principles. The Social Insurance and Public Finance Section provides an opportunity for a constructive exchange of ideas and improved understanding of how social insurance and other government-sponsored programs may differ from seemingly similar private ones.

Our section is active in diverse projects and has been expanding its collaboration with other sections. We sponsored two sessions at the 2015 SOA Annual Meeting & Exhibit, one on actuaries' responsibility to the public and one on assumptions and methods used for Social Security estimates. We also co-sponsored a hot breakfast with the Health Section, our first in an Annual Meeting. By the time this newsletter is published, we will have held a webinar on Medicaid Long-Term Services and Supports, from our health sub-group, and one on global social security reforms in collaboration with the International Section. We are also planning a webinar on Social Security's Disability Insurance program, and the effect of recent legislation, early in 2016. Other ongoing projects include a long-term care research project with a focus on funding, challenges and potential alternatives and their impact on Medicare and Medicaid, as well as a research project to investigate funding issues of long-term health benefits for retirees in the public sector. We also continue to look into public pension issues.

If you have interest in these ongoing projects, or ideas for new ones, the section would welcome your participation. ■

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