The Actuary

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THE Actuary

Membership survey reveals attitudes and opinions

by Philip Kuehl
and Chelle Brody

In mid-September 1992, the Society of Actuaries commissioned Westat, Inc., a large U.S. survey research firm, to conduct a telephone survey among a random number of members. The survey's purpose was to assess general attitudes, evaluate member perceptions of current and potential programs, and define opinions on future strategies. A total of 600 respondents (273 Fellows and 327 Associates) participated. Canadian members were represented in the survey in the same proportion as membership. No overseas calls were made.

General effectiveness

In general, the survey concluded that the Society can plan for the future from a position of organizational strength. Overall, members believe the Society is effectively implementing its strategies and producing high calibre new members. The Society is perceived as providing good value for member dues. This suggests that the Society should continue with evolutionary strategies as it advances the profession and serves its members. Revolutionary strategies can be used for immediate response to significant changes in the profession.

More than 86% interviewed think the traditional roles for the Society of Actuaries (research and education) and for the American Academy of Actuaries (public policy and governmental issues) are appropriate.

As hoped, the survey results pinpointed some areas for improvement.

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Social Security discussion continues

by Cecilia Green,
with editorial assistance from
Dick Bilisoly and Mary Riebold

Over the years, *The Actuary* has presented the ongoing debate on the financial soundness of the U.S. Social Security system. This past year proved to be an especially "meaty" one, highlighted by the publication of A. Haeworth Robertson's newest book, *Social Security: What Every Taxpayer Should Know*. The September *Actuary* carried an article by Robertson, "Social Security's uncertain future," and the October issue included a review of Robertson's book by Robert J. Myers. Myers was Social Security's chief actuary from 1947-1970, and Robertson held the same post from 1975-1978.

These events triggered a group of letters of support, challenge, or elaboration. This article provides excerpts from these letters, weaving them into a summary discussion. The respondents, many of whom have professional experience with Social Security financing issues, are:

- Eric J. Klieber, an actuary at W F Corroon in Cleveland and the principal author of the outside review of the 1991 and 1992 valuation of the Social Security OASDI system performed by the Office of the Actuary.
- Robert A. Gilmour, president of the American Institute for Economic

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In this issue:

Discussion cont'd

Research in Great Barrington, Massachusetts
- John F. Hook, a retired member of the Society of Actuaries
- William Sutton, actuary at Provident Mutual Life Insurance in Philadelphia
- Edwin C. Hustead, senior vice president at Hay/Huggins Company in Washington, D.C., who has worked with the Congressional Research Service on the analysis of Social Security issues. He also was the chief actuary of Personnel Management for the federal government, which deals with the Civil Service Retirement System;

and, of course, Robertson and Myers. Each voiced his comments on the key issues that frame the debate.

Is 75 years too long a projection period?

Eric Klieber believes that Robertson "sounds a timely warning" and suggests that the 75-year valuation system be reduced to 25 years. The following paragraphs are a summary of Klieber's written remarks:

"[Robertson cautions] against relying on the Social Security program to provide the same level of retirement benefits to the current generation of workers that the program is providing to current retirees. However, by narrowly focusing on the monetary value of contributions and benefits and ignoring the social and economic context in which the program operates, he paints an excessively gloomy picture of how Social Security will contribute to future retirees' financial security.

"Robertson claims that, under any reasonable set of assumptions, a very large gap will occur between projected income and outgo. In a [technical] sense, this is true. . . . Without a dramatic upsurge in worker productivity, the inevitable result is an overall decline in the standard of living for working Americans. I question whether a set of assumptions under which Congress props up the standard of living for retirees by maintaining the current Social Security benefit structure in the face of declining living standards for workers can be considered 'reasonable.'

"I am not predicting a declining standard of living during the next century. I see three possible scenarios for the future of the American economy:

1) Worker productivity does not increase sufficiently to offset a decline in work force participation, resulting in a declining standard of living.
2) The decline in work force participation raises the cost of labor relative to capital, leading employers to invest in labor-saving equipment, thereby raising worker productivity enough to maintain current living standards.
3) Employers provide sufficient incentives to entice workers to postpone retirement, thereby preventing a decline in work force participation and maintaining current living standards.

"Robertson touches on the third scenario . . . , although he treats postponement of retirement as a unilateral decision by the worker, rather than a mutually advantageous arrangement for . . . worker and employer.

"These scenarios are not mutually exclusive. Most likely, the future will bring some combination of the three, but how much weight each will carry, no one can tell now. The important point is that, under any of these scenarios, the promises of Social Security can be kept if these promises are properly understood.

". . . Congress is free to change the [current] benefit formula and retirement age at any time and will do so if necessary to maintain the integrity of the system. . . . This is not [to say] that Social Security will not keep its promises to future retirees. The real promise of Social Security is that working Americans will share a portion of the product of their labor with retirees to enable them to maintain a standard of living commensurate with the working population. . . .

"A good case can be made that a defined benefit formula is not the most efficient way to ensure that benefits of retirees stay in line with the wages of workers. . . .

"These considerations cast doubt on the value of the current practice of assessing the viability of retirement benefits provided by Social Security on the basis of the annual 75-year valuation of income and outgo. The 75-year period was chosen because it encompasses the future lifetimes of most workers entering the system at age 22 in the valuation year. While the development and operation of the 75-year valuation system represent a major technical achievement, two shortcomings render the valuation results of little practical value:

1) Uncertainties regarding economic and social trends make any 75-year projection a matter of pure speculation. Finessing this problem by simply assuming the current plan of benefits will remain unchanged and that current social and economic trends will continue indefinitely leads to internal inconsistencies. Yet any predictions regarding changes in economic and social trends or changes in the benefit formula are no less speculative.
2) Asking Congress to shape policy based on projections of financial problems decades into the future is unrealistic. Further, in my view, for Congress to shape policy based on such speculative results would be irresponsible.

"[Several compromise solutions have been suggested.] Francisco R. Bayo [deputy chief actuary of the Social Security Administration] has suggested applying to each year's projected income and outgo an exponentially decreasing 'relative reliability factor'. . . . Dwight K. Bartlett [chief actuary of the Social Security Administration from 1979-1981] has suggested changing the tolerance band that defines close actuarial balance, currently a 5% discrepancy between income and outgo over the valuation period, to 5% for the first 25-year period, 7.5% for the first 50-year period, and 10% for the first full 75-year valuation period. . . .

"I suggest instead that the annual valuation of the Social Security program be limited to a 25-year period. The 25-year period is not based on a belief that social and economic trends can be accurately projected even this far into the future (no past valuation of Social Security has proved accurate over so long a period), but on a practical approach to congressional oversight of the system. Under a 25-year valuation, incoming senators and representatives in the first year a future deficit is detected will have the opportunity to study the evolving financial situation first-hand. They will have time to move into leadership positions and shape corrective legislation before insolvency ensues.

"Experience shows that, in the face of crisis, Congress usually fashions solutions that reflect a broad consensus of the population. In the case of Social Security, this means setting tax rates and benefit levels to provide workers and retirees with a roughly equivalent standard of living, whatever that may be at the time taxes and benefits are adjusted.

"One might argue that a program requiring major disbursements of accumulated tax dollars into the indefinite future should be funded as far in advance as possible. However, many federal programs are highly likely to require major expenditures of tax dollars for the indefinite future, such as national defense, income supplementation for the poor, and funding for highways and other infrastructure. . . . The only reason for not appropriating funds for Social Security on a year-by-year basis like most other federal programs is the unwillingness of Congress to deal regularly with this sensitive issue.

"A 25-year valuation period represents a reasonable compromise between the credibility of the valuation results and the desire of most members of Congress to deal with the Social Security issue at most once during their terms in office.

"The 75-year valuation system can still be a useful tool for long-range forecasting and research. Over the past decades, social and economic trends which at the time may have been imperceptible have combined to produce major changes in our society. There is little reason to believe society will not continue evolving over the next 75 years. Therefore, efforts should be made to identify trends that could affect the long-term financial viability of the Social Security program and to study their potential effects."

Economist says basics should not be overlooked

After Myers' November 1992 letter to the editor responding to Robertson's October article, Robert Gilmour reminds us of the economic fundamentals involved. He gives the following example: "In reference to Social Security's 'purchase' of [non-negotiable] Treasury securities, [Myers] asks, 'How is this any different than [*sic*] . . . when a person puts money into a savings account, and the bank 'spends' the money by lending it to somebody else?'"

Gilmour asserts it is very different. "Banks and other private financial intermediaries do not 'spend' deposits. . . . Rather, they invest them in loans and require tangible collateral be provided against the possibility of default. [If] the loan defaults, the collateral can be liquidated to satisfy the debt."

Holders of non-negotiable Treasury securities do not have this recourse, because the only "collateral" under present arrangements is the taxing authority, Gilmour writes. "What disturbs Mr. Robertson and others is what may happen when such 'collateral' proves inadequate, i.e., when the proportion of taxpayers to beneficiaries is inadequate either to continue to fund Social Security's revenue requirements or to service the government's aggregate debt load, which would mean the government would no longer be able to borrow."

Is social insurance a doomsday machine?

John Hook, a retired member receiving Social Security benefits, wrote that he is puzzled by the term, "fallacious," that Robertson and other writers have applied to the Social Security trust fund.

"Is there really a likelihood that the United States will not honor its Treasury bond obligations and its moral obligation to apply Social Security tax receipts to fund the Social Security system?" he asked. "Obviously, government accounting reports that ignore this obligation are fallacious, but that doesn't seem to erase the obligation."

Hook names several groups that are not satisfied with the system and who may not support its continuation in the current form:

- Those who believe they should have more benefits, such as the "notch baby" group
- Those who pay FICA taxes. Hook thinks total taxes for middle income people, including FICA taxes, are widely believed to be unfairly high and that political action to lower either income taxes or FICA taxes is likely.
- Employers who dislike increasing payroll taxes and increasing costs of other employee benefits

"Social insurance has the appearance of a doomsday machine," Hook wrote. "Many beneficiaries, generous benefits, taxpayer resistance, and little prospect of responsible reform support that appraisal."

Robertson responds to review

Myers' October review of Robertson's new book included the statement that Myers has a list of 43 factual errors and omissions that he would supply to readers upon request. The following is a portion of Robertson's response:

> "Anyone who is concerned about [my] book's accuracy should certainly obtain the list. It points out such errors as (1) The 'sexist nature' of a quotation from a Society of Actuaries' publication defining an actuary, because it uses 'he' instead of 'he or she.' (2) Footnote 2 on page 304 failed to mention the spouse-government-pension-offset provision. (3) On page 132, I referred to the Veterans' Benefit Administration, and [Myers] believes I should have said 'Department of Veterans Affairs.' In fact, the Veterans' Benefit Administration is a subdivision of the Department of Veterans Affairs, just as the Social Security Administration is part of the Department of Health and Human Services.
>
> "What a relief that Myers did not challenge my assertions that both OASDI and HI are not adequately financed for the baby-boom generation, and that taxpayers should be made aware of this in time to take corrective action. Neither did he challenge my assertion that the so-called 'trust funds' do not have real assets and that they represent merely an intention to collect additional general revenue in the future."

Myers responds to Actuarial Update article

Robertson's article, "Forecasting a

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Discussion cont'd

Fiasco," in the American Academy of Actuaries September 1992 *Actuarial Update* prompted a rebuttal from Myers, saying that his "doom and gloom" picture is incomplete. Myers says Robertson does not separate OASDI and Medicare. "OASDI provides cash benefits bearing measurable relationships to past earnings. Medicare provides reimbursement for health care services, which do not have precise utilization limits. Thus, . . . the real culprit is Medicare," he writes.

He further explains that the "fiasco of horrendous costs" about which Robertson warns us will not come overnight, so necessary changes can be made gradually as the experience develops.

Nothing new in the SS debate in 10 years

Edwin Hustead comments, "The Robertson-Myers debate on Social Security has not offered us anything new for a decade." The following edited paragraphs from his letter explain his views:

"Yes, Haeworth, we know that the total Social Security/Medicare tax rate falls far short of the future needs of the combined program. Yes, Bob, we know that the Social Security tax rate is almost adequate for the future needs of the Social Security program without Medicare. In that view, either unpredicted changes in the economy will balance the income and outgo, or minor adjustments will be made to taxes or benefits in the next millennium. We decide whether or not to include Medicare with Social Security and then march hand-in-hand with either Myers or Robertson. For the rest of this letter, I will simply refer to Social Security and let the reader decide if that includes Medicare or not.

"The issue that Myers raises in the November 1992 *Actuary* also is old, but it is much more complex than the rest of the argument. It is important for actuaries to understand and appreciate the political and economic implications of the Social Security trust fund investments. It is the real-world financing of Social Security, and not the artificial world of the trust funds financing, that has driven and will drive the debate on this issue.

"Perhaps Robertson's use of 'fallacious' in describing the trust funds is overly strong, but he is correct. Everyone who really understands the operations of the federal budget agrees with him. Social Security tax revenues are in fact spent when received, and current year benefits are in fact funded by current year taxes. The current excesses are spent on other federal programs. When Social Security outlays exceed revenues, the government will have to meet that year's Social Security deficit from other sources, such as increased taxes or reduced spending.

". . . The illusory nature of the trust funds explains the debate on Social Security benefits. If the trust funds had a real economic meaning, then no advantages to cutting Social Security benefits this year would exist. No one would propose cutting those benefits, and politicians would not fall all over each other swearing not to cut benefits. As Social Security payments make stronger . . . demands on the federal budget, the generational debate will center around how much can be paid each year out of that year's taxes. The size of the trust fund balance will be meaningless."

Din of inequity

Bill Sutton reminds us of the 1959 paper, "Misconceptions and Missing Perceptions in Our Social Security System (Actuarial Anesthesia)" by Ray M. Peterson (*TSA* XI, p. 812), that was on the examination syllabus for several years. Peterson believed that as employee contribution rates increased to an amount more than the value of employees' own future benefits, resistance to paying those rates would occur. As a result of this, he wrote, "There will truly arise a din of inequity."

Sutton commented, "My feeling is that Robertson, in his own way, is trying to create a modern version of Peterson's 'din of inequity' which never did arise."

More discussions by actuaries available

Session 86, "Worldwide Social Security Programs," at the Society of Actuaries October 1992 annual meeting in Washington, D.C., was moderated by Bob Myers. Panel members represented U.S. and other governmental agencies. They discussed social insurance systems in Canada, Latin America, Eastern Europe, and Asia. Audio tapes are available through Teach'em Inc., 1-800-225-3775, and the session will be printed in the Society's *Record*, to be published in late 1993.

Another discussion appears in "Sooner than You Think — the Coming Bankruptcy of Social Security," an article by SOA member Bruce D. Schobel published in the fall 1992 issue of *Policy Review.*

Nineteen ninety-three and the new administration should provide fertile new areas for continuing the Social Security discussion.

Cecilia Green is staff editor and Dick Bilisoly is education actuary at the Society of Actuaries. Mary Riebold is managing director of the William M. Mercer New York office, a member of the SOA Board of Governors, and the immediate past president of the Conference of Consulting Actuaries.

NAFTA cont'd

work done on developing a common code of conduct between Canada and the United States. How that code could be applied in Mexico, as well as what the current Mexican actuarial code of conduct offers, should be considered, he said.

The strong licensing and accreditation system present for Canadian and Mexican actuaries may make it easier for them than for the United States to join in a reciprocal accreditation package, McCrossan said.

"Whatever we design has to be expandable," McCrossan said. "NAFTA is an open-ended treaty. Any new entrants that apply can join if they accept the terms of the treaty. That means that whatever we decide not only has to work between Canada, Mexico, and the United States, it also has to be capable of expansion into Chile, Argentina, Brazil, Australia, and New Zealand, who have indicated some interest in joining NAFTA."

McCrossan also mentioned the professional issue of how involved actuaries in the three countries would be in leading governments through "the most difficult sociological problems they all face" — the problem of the aging population.

"This is a worldwide problem," he said, "and one where NAFTA and the professional cooperation among the three groups may offer something to their countries."