

January 2008, Issue No. 66

IN THIS ISSUE

Chairperson's Corner

"Rename the PSN" Contest Rules

Report from the 2007 Retirement 20/20 Conference: Aligning Roles with Skills

SOA Releases New Long-term Health Care Cost Trends Resource Model

Information Sources for DB Plans Outside the United States

PPA...Ready or Not

A Pension Section News Book Review: Annuity Markets and Pension Reform

Some Interesting Information about Phased Retirement

In Defense of Assumptions and Methods

Return to Email Version

LINKS



Pension Section Council



20 / 20 Web site



Contact the Editor



Calendar of Events

EVENTS

A PENSION SECTION NEWS BOOK REVIEW: ANNUITY MARKETS AND PENSION REFORM

Michael B Price, ASA

The reader of *Annuity Markets and Pension Reform* by George A. (Sandy) Mackenzie might infer from the book title that this book somehow directly relates to U.S. legislation, Pension Protection Act enacted in August 2006. To the contrary, Sandy Mackenzie's work takes us well beyond today's political fixes or non-fixes of the U.S. defined benefit system. This book provides the basis for a new generation of benefit delivery in this country, as the "grip of public pension systems on the annuity market is now loosening." While not intended to solve every issue that must be addressed to create a viable and efficient annuity market, Mr. Mackenzie does cover many related practical considerations. It is no surprise, considering the author's background as an economist, that the book is written from an economic policy perspective, rather than from the mathematical detail of an actuary or social policy of a bureaucrat. It avoids detailed treatment of the current political climate in the United States which will keep this text fresh in its analysis and opinions regarding annuities for many years.

This is a very readable book, void of the usual plethora of formulas you would expect from such an academic work. Most formulas are relegated to an appendix. There are many references for those desiring more detail on much of the underlying theory and research quoted. The book is organized such that the reader is provided a warm-up history of annuities, followed by a guide to the book and chapter outline. The substantive material is divided into two parts. Part one, "introduces and develops the subject of annuities." Part two, "addresses policy toward distributions." Both parts compare the current U.S. annuity system with those of other countries. The author's conclusions are heavily influenced by past and current practices of other nations. Particular attention is given to Chile's individual account system, which reflects Mackenzie's experience with advising South American governments on individual account reform.

The book has "two main objectives." First, for public pension systems that plan to implement individual account reform, it provides a guide to the policies that should govern and regulate distributions from individual accounts. Second it considers the adequacy of the regulation and supervision of the annuity business, and how private annuity markets might function more efficiently. Mackenzie is specifically concerned with rules that govern the distribution side, touching on which design aspects might be voluntary and which mandatory. Based on the research of various academicians and economists, and his own opinions, Mackenzie provides insight into the reaction of the annuity marketplace, both private and public, both provider and recipient to various aspects of current policy such as taxation, adverse selection, mandatory v. voluntary distributions. For example, he points out that M.E. Yarri has developed a model that shows that under certain assumptions people would invest in annuities and

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nothing else. However, the private annuity market is small in most countries. Mr. Mackenzie explains this paradox in the U.S. through discussion of contributing factors, such as the desired level of consumption in retirement, the desire to leave a bequest, and the tax-favored status of other investment vehicles among other factors.

The book begins by "posing three basic questions." (1) What should the policy towards distributions from individual accounts be? (2) Should annuities be provided by the private or public sector? (3) How can voluntary annuities be made more efficient and regulation ensured? While McKenzie provides his insight into the issues to be tackled in order to develop answers for these questions, I believe that he avoids the one-size-fits-all approach to his conclusions. For example, he notes that we, in the United States, put high value on the private property aspect of individual accounts. This is in sharp contrast with other countries. Other countries put much greater emphasis on the aspect of retirement security. Similarly, choosing the optimal degree of annuitization may better suit one class of individual than another, depending on the individual's "wealth, taste for risk, financial acumen, and life expectancy." The point here is that this book will give the reader the fundamental knowledge to formulate his or her own answers to Mackenzie's basic questions, depending on the geography, demographics, politics and time in history under consideration.

That fundamental knowledge is provided within a number of concise chapters. Each chapter provides a building block leading to a final chapter of conclusions and recommendations that clearly evolve from Mackenzie's perspective developed from his work with international annuity schemes. There is much to learn from the balance of "compulsory annuitization and laissez-faire," and a combination of public and private administration, that is featured in the annuity systems of other countries.

Annuity Markets and Pension Reform
George A. (Sandy) Mackenzie
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248 pages

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