



SOCIETY OF ACTUARIES

Article from:

Pension Section News

September 2004 – Issue No. 56

Chairperson's Corner

by Ian Genno

The spring and summer have been busy and productive periods for the Pension Section Council. We have continued our initiatives to deliver services to section members in the form of research projects and tools, publications and meetings/seminars. Council members have also participated actively in ongoing discussions regarding the future organizational structure of the SOA, focusing on identifying the most important services to support pension practitioners and how those services can be managed in the most effective way. Here's a quick summary of what we've been doing on your behalf.

Research

Work has been completed on an important new software tool that will help pension actuaries address the "risk of ruin" for individual pension plan members. In an environment where individuals are increasingly called upon to manage their own assets during their retirement years (because of the increasing prevalence of defined contribution plans, as well as lump sum payouts of defined benefit entitlements), the risk of depleting one's retirement savings prematurely can be significant. Traditional approaches for managing this risk included buying an annuity (which many retirees unfortunately regard as an undesirable option) and seeking the advice of a financial planner (which often involves testing several sets of investment return and lifespan assumptions, on a deterministic basis). Working with several members of the Pension Section and the Individual Life Insurance and Annuity Product Development Section, Moshe Milevsky (a faculty member in the business school at York University in Toronto) has built a practical tool to enable actuaries to address the risk of ruin for individuals managing their own retirement assets using robust stochastic methodologies. The software and related documentation are on the SOA Web site at <http://www.soa.org/lccm/content/areas-of-practice/special-interest-sections/pension/retirement-probability-analyzer-software> — take a look! While, at first blush, one might think that this issue is only of relevance to actuaries who work directly with individuals to provide financial planning services, it in fact can be very useful to actuaries working with pension plan sponsors. By helping plan sponsors understand the

risks faced by members who cash out lump sums, and the risks faced by members with defined contribution coverage, we can help develop better employee education and communication programs as well as better plan designs, and have a better understanding of the actual mechanics of converting a lump sum at retirement into an ongoing income stream.

We are also pursuing several other research initiatives — some of which are intended to provide practical information or tools with immediate application for pension practitioners, and others which are envisioned to offer some "blue sky" thinking on topics of longer term importance to the pension community:

- Retirement rate assumptions: As a follow-up to the 2003 SOA pension plan turnover study, we believe it would be helpful for actuaries to have some general guidance on the selection of retirement rate assumptions. Building generic tables of retirement rates (similar to tables for disability, termination and mortality rates) can be a fruitless exercise because of the myriad of factors that vary from one pension plan to another — including differences by industry, work environment, pay level, pension formula, early retirement provisions, availability of postretirement benefit coverage, current economic conditions, etc. Instead of building traditional tables, we plan to review current literature on the subject, test several hypotheses against available data and develop a summary that offers actuaries some guidance on the selection of retirement rate assumptions and the associated implications.
- Pre-retirement influences: On a related note, Linda Smith Brothers, ASA at the University of Wisconsin is currently conducting a literature search to explore the various factors that influence an employee's decision to retire.
- Phased retirement: A team of experts from the academic and consulting communities is being assembled to explore phased retirement, with a view to developing practical recommendations for implementing programs in the current regulatory environment. After brainstorming in the summer, the team will propose initiatives

(continued on page 13)



Ian Genno, FSA, FCIA, is a principal with Towers Perrin in Toronto. He can be reached at Ian.Genno@TowersPerrin.com.

Pension Section Council Contacts:

Anne M. Button, FSA anbutton@deloitte.com
Secretary

Betsey Byrd, ASA betsey.byrd@watsonwyatt.com

Arthur L. Conat, ASA art.conat@ey.com

K. Eric Freden, FSA efreden@segalco.com

C. Ian Genno, FSA, FCIA
ian.genno@towersperrin.com
Co-Chair

Ken Kent, FSA, ken.kent@mercer.com

Tonya Manning, FSA, tonya_manning@aoncons.com
Vice-Chair and Pension Section News Liaison

Mike Pisula, FSA, mpisula@msn.com
Treasurer and SOA Spring Meeting Pension Program Liaison

Sarah W. Wright, FSA, swright@segalco.com
Co-Chair

for the median (50th percentile) and for the 95-percent and 80-percent confidence intervals. For comparison, deterministic estimates are shown for the intermediate, low cost, and high cost assumptions. Each stochastic estimate displayed in the table does represent the results of one stochastic simulation. However, for a given percentile, the stochastic estimates shown for the different long-range actuarial measures are generally not from the same stochastic simulation.

Hypertext versions of the 2004 Social Security and Medicare Trustees Reports as well as “A Summary of the 2004 Annual Reports” are available on the Internet at the following addresses:

Social Security (OASDI):<http://www.ssa.gov/OACT/TR/TR04/index.html>

Medicare (HI and SMI):<http://www.cms.hhs.gov/publications/trusteesreport/2004/>

Summary:<http://www.ssa.gov/OACT/TRSUM/trsummary.html>

Other information about Social Security benefits and services is available at: <http://www.ssa.gov> or by calling toll-free 1.800.772.1213

Other information about Medicare benefits and services is available at: <http://www.cms.hhs.gov> or by calling toll-free 1.800.663.4227. ♦

Chairperson's Corner • from page 3

for the Pension Section Council and the Research Committee to consider.

- Solving the portability problem: The Pension Section Council is considering a call for papers to identify potential solutions to address the various practical problems facing plan sponsors and members relating to portability of pension benefits.
- Cash balance plan survey: The Research Committee is preparing to conduct a comprehensive survey of cash balance plans in the United States, examining a variety of aspects including prevalence, design, transition, financing, and communication.
- Rational retirement age: The notion of age 65 as the “normal retirement age” dates back to the 19th century, when life expectancies were far shorter than today. In addition to longer life expectancies after retirement, employees approaching retirement age today are healthier, working conditions are significantly different and individuals' economic needs during the years leading up to and immediately following retirement reflect different priorities and commitments to dependent children and elderly parents. These considerations call into question the relevance of age 65 as the pivot point for private and public retirement plans. To help support future discussion within the broader community of legislators, plan sponsors and the general public, we believe that some basic research could help bring greater intellectual rigor to the question of what the right retirement age is. This could take into account macroeconomic and societal issues, questions of affordability of retirement, and methodologies for the qualitative and quantitative assessment of an individual's ability to work productively (e.g., applying approaches used to assess the ability to work for individual claimants under disability plans, on a broader population basis).

- “Paternalism versus orphanism”: From studying for actuarial exams (and, for those of us with a few grey hairs, from design work with plan sponsors in decades past), we're all familiar with the concept of paternalism as a rationale supporting employers' fundamental design, communication and management decisions for pension and postretirement benefit plans. In recent years, however, employees have increasingly demanded greater control over their own financial security, and many employers have expressed concerns over their ability and responsibility to provide full, automatic, guaranteed benefit coverage and protection to employees and retirees. As the pendulum swings toward greater autonomy and self-reliance for individual employees and retirees, what are the longer term financial and societal implications? Is there a risk that the pendulum could swing too far—and, if so, what are the consequences? The Pension Section Council has contemplated this “blue sky” question, and is starting to reach out to others outside the actuarial community to spark some discussion and debate.

Publications

Several items are being developed for publication—in some cases, in traditional print form; in other cases, electronically:

- *Pension Forum*: Two issues of the *Pension Forum* are confirmed for release this year—one focusing on the bond yield curve (with perspectives on how yield curves are developed and practical aspects of using yield curves to value pension liabilities), and another centered on ASOP 27. A third issue will follow as soon as practical, to highlight the remaining papers from the 2003 Financial Economics Symposium that have not yet been published in other journals.

(continued on page 14)

- Web site for the general public on retirement issues: Employer-sponsored retirement plans can be difficult for the general public to understand. Yet such plans are an integral component of the U.S. and Canadian retirement systems. An enhanced public understanding of how typical plans are designed and delivered could contribute to their future growth and sustainability. The Pension Section Council is exploring the feasibility of developing and supporting a Web site for the general public that would provide simple, understandable information on issues relating to the delivery and security of retirement income (including employer-sponsored plans). While further discussion is still required to confirm the intended content in more detail, we anticipate the Web site may include information on topics such as the various ways that

webcasts offered by the SOA, CIA, CCA, etc. Our goal is to find the most effective way to offer pension actuaries value-added continuing education opportunities that are clearly distinct from other available alternatives.

Our initial conclusions are that we should move away from offering a broad "cafeteria style" array of session topics at SOA meetings, in favor of sponsoring:

- An increased number of webcasts on topics of current interest (which are easier and more cost effective for actuaries to attend, and are quicker and less expensive for the SOA to organize), and
- One or two seminars that focus on specific topics in depth, embedded within the traditional SOA Spring or Annual Meeting. (This will ensure we continue to offer actuaries an opportunity to attend face-to-face meetings for networking purposes as well as to participate more fully in discussions and debates than is feasible through a webcast. Our focus, however, will be to ensure that the seminar content is sufficiently distinct from other actuarial organizations' meetings, and is of appropriate depth for a more experienced audience.)

We are currently planning several upcoming webcasts, and envision embedding a symposium at the 2005 Spring Meeting on the practical application of financial economics in pension consulting.



retirement income can be provided, the types of risks associated with different retirement plan designs, the concept of the time value of money, investment and longevity risks, etc. Once the scope and feasibility of this initiative have been explored more fully by a working group, the Council will make a decision on whether and how to proceed.

And, as always, we continue to publish the Pension Section News on a quarterly basis, to provide letters and short articles on topics of current interest, presented in a practical, easily digested and non-academic manner.

Meetings and Seminars

Following the SOA Spring Meeting in Anaheim, the Pension Section Council has reviewed feedback from this year's attendees as well as general trend information on Spring Meeting attendance. We have discussed the type of content that employers and pension actuaries are asking for the most, the time and cost constraints that many actuaries face, and the variety of other meetings, seminars and

Governance

Although our energies have primarily been focused on the initiation of relevant research and continuing education services to Pension Section members, Pension Section Council members have also participated actively in the SOA's governance review and organizational restructuring. Although (at the time of writing this article) it is still too early to describe exactly what the new SOA structure will look like for pension actuaries, we are confident that it will be more streamlined and more accessible than the current structure, and that the Society's ability to deliver value-added services to pension actuaries will be enhanced even further. The Pension Section Council, the Retirement Systems Practice Advancement Committee, and the various retirement-related SOA committees and task forces have an enviable track record of accomplishments which we believe can be preserved and enhanced even further. We expect you'll see more news on this over the balance of this year and early in 2005.

So ... the spring and summer have been busy and productive periods for the Pension Section Council! We hope you are continuing to derive value from the Society's services to pension actuaries, and we continue to welcome your comments and suggestions on how we can serve you better. ♦