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Pension Section News

Defined Benefit Plans vs. Defined Contribution Plans

by Mark Ruloff

Employers and investors have suffered recently from taking too much investment risk inside their defined benefit (DB) plans, producing calls for more transparent accounting. Some employers have tried to eliminate this pension risk by moving to defined contribution (DC) plans. However, this is not the only, or even the best, option available.

Move to Defined Contribution Plans

Many plan sponsors see moving to DC plans as a way to reduce the investment risk. However, the risk is not actually reduced but shifted to employees. In fact, the risk actually increases.

Bad for participant

The shift to DC plans passes the risk to the participants, who are far less able to manage it than shareholders and lenders. Participants lack the connections and resources to get the same quality of investment advice available to a large DB plan. The participant also now has a longevity risk which was less in the DB plan due to the pooling of individual risks.

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Chairperson's Corner

by Ian Genno

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As we enter 2005, the world continues to be an exciting place for actuaries practicing in the retirement field. We are collectively engaged in what is arguably some of the most interesting and challenging work facing anyone in the actuarial profession today—addressing the income and security needs of current and future retirees. We work in an environment of increasingly complex regulations, volatile investment markets, interest rates at historically low levels, increased job mobility, lack of understanding among pension plan members and litigation. This environment has prompted some employers and plan members to re-examine the value and viability of pension plans—and it has created important opportunities for retirement practitioners to help plan sponsors, plan members, legislators and regulators understand the issues and make informed decisions that will directly affect the future financial well-being of millions of people.

Retirement actuaries are supported by several professional organizations—the SOA, CIA, AAA, CCA and a variety of other national actuarial organizations around the world—each playing complementary roles to help address practitioners' needs. For the SOA—with its focus on actuarial research and professional education—the Pension Section represents the needs of nearly 4,000 FSAs and ASAs practicing in the retirement field, providing leadership in the development and delivery of practical research initiatives, technical tools and continuing education opportunities. As we enter 2005, the SOA's new, streamlined governance structure will also enable the Pension Section to provide input on basic education for actuarial students, and to work even more closely with some of the SOA's special interest groups (dealing with issues such as financial economics, postretirement needs and risks and Social Security).

The Pension Section accomplishes its work through the effort and commitment of SOA staff and numerous volunteers. One group of volunteers is the Section Council, whom you elect each year. Each fall, three new council members join the team, bringing new energy and fresh perspectives to the table. By the time this edition of *Pension Section News* is published, the recently elected members will already have stepped into their new roles and started working on 2005 priorities for the section.

Joining the council for three-year terms are Josh Bank, Tammy Dixon and Martine Sohier. Welcome!
Josh (who practices with Deloitte in New York) brings a multidisciplinary and multicultural perspective to the table, his experience including work both in the insurance and benefits arena. This experience has exposed him to public and private pension issues in the United States, Southeast Asia and South America. One of his key interests in serving on the council is to help the SOA address some of the fundamental retirement income security challenges facing North America in the coming quarter century.

Tammy (employed with The Segal Company in Los Angeles) offers the council a breadth of experience, having worked over the years in a variety of settings: an insurance company and small local, mid-size national and global consulting firms—enabling her to view the pension world and understand the needs of Pension Section members from various perspectives.

Martine (who recently moved to Watson Wyatt in Toronto) has extensive Canadian pension experience, which will help ensure that the council considers pension issues in a broader North American context—particularly important, given the significant number of SOA members in Canada, and an historical tendency for Canada to be on the forefront of developments in pension jurisprudence, legislation and design trends.

At the same time, three members are retiring from the council: Eric Freden, Sarah Wright and me. Speaking on our behalf, we thank you for offering us the opportunity to help the SOA serve the needs of retirement practitioners, through the Pension Section Council's role in developing and delivering practical research initiatives, technical tools and continuing education opportunities. Our three years on the council seem to have flown by quickly, and we've each enjoyed the opportunity to help contribute, in some modest way, to benefit our fellow retirement practitioners as well as to advance our profession.

Good luck to the new (and continuing) members of the council—and to all retirement practitioners facing exciting challenges and opportunities in 2005. ◆

SOA Elections: Do Retirement Practitioners Use Their Voices?

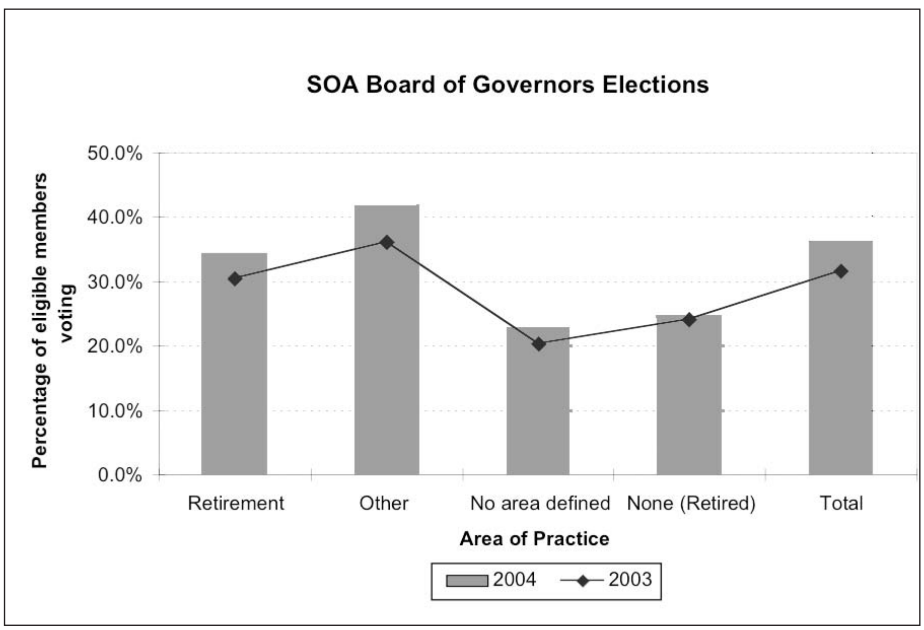
by Emily K. Kessler

In his June 2004 Chairperson's Corner, Ian Genno suggested several methods whereby retirement practitioners might get involved with the SOA. One was simply to vote in the 2004 SOA Board of Governors elections. In his piece, Ian noted that only 30.4 percent of members who identified their area of practice as "retirement" voted in the 2003 elections.

So, what was the actual percentage of retirement actuaries voting in the 2004 elections? The good news is that participation by all actuaries, including retirement actuaries, increased. In 2003, 31.7 percent of eligible voters participated in SOA Board of Governor selections; in 2004, 36.4 percent of eligible voters participated. (Participation in SOA elections has increased since the introduction of electronic voting.)

However, the bad news is that retirement actuaries—although they voted in larger numbers—are still voting less often than their peers. In 2004, the percentage of retirement actuaries voting increased from 30.4 percent to 34.4 percent. But, among most other actuaries still active in the profession, the number of eligible actuaries voting jumped from 36 percent to 41.7 percent. Retirement actuaries continue to vote less often than their peers except for two groups: those actuaries who don't identify an area of practice (often because they've left the profession) and those who are retired. The chart below summarizes who actually voted in the 2003 and 2004 Board of Governors elections—statistics are different for section elections.

Area of practice is the primary area of practice as self-reported by members in the SOA online directory. Other areas of practice include academic, finance, financial reporting, general management, health, investments, life, nontraditional, property and casualty, regulatory and reinsurance. ◆



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In Depth: Summary of 2005 IRS, PBGC, Federal Income Tax, Social Security and Medicare Amounts

by Heidi Rackley, Scott Tucker and Fran Bruno of Mercer Human Resource Consulting

December 8, 2004

This article summarizes 2005 cost-of-living adjustments related to employee benefit plans, including: (i) IRS limits applicable to retirement plans, transportation fringe benefits, adoption assistance programs, medical savings accounts, health savings accounts, high-deductible health plans and long-term care plans; (ii) PBGC guaranteed benefits; (iii) federal income tax factors; (iv) Social Security and Supplemental Security Income; (v) Medicare and (vi) covered compensation.

IRS Retirement Plan Limits

Most 2005 retirement plan limits will increase from their 2004 values, either because they are set to increase by statute or because the 2.73 percent increase in third-quarter CPI-U from 2003 to 2004 was sufficient to increase the rounded limit. The IRS published the 2005 rounded limits in an October 20, 2004, news release. Table 1 on page 5 shows the rounded and unrounded 2005 limits and the prior three years' limits.

Other Employee-Benefit-Related IRS Limits

The 2005 Internal Revenue Code limits for qualified transportation fringe benefits, qualified adoption assistance programs, medical savings accounts (MSAs), health savings accounts (HSAs) and high-deductible health plans (HDHPs) reflect the 2.3 percent increase in the average CPI-U for the 12 months ending August 31. Limits for qualified long-term care premiums and per diem amounts reflect the 4.4 percent increase in the medical care component of CPI-U from August 2003 to August 2004. The IRS published the 2005 rounded limits in Rev. Proc. 2004-71. See Table 2 on page 6.

PBGC Guaranteed Benefits

The maximum PBGC guaranteed monthly benefit is adjusted annually on the basis of changes in the Social Security "old law" contribution and benefit base. For a single- employer defined benefit plan terminating in 2005, the maximum guaranteed benefit will be $3,801.14 per month—a 2.8 percent increase over the 2004 limit of $3,698.86. This amount is adjusted if benefit payments start before age 65 or if benefits are paid in a form other than a single-life annuity. Some of the guaranteed amount may be paid from the plan's assets, and participants may receive more if the plan is better funded or the PBGC can recover other amounts from the plan sponsor.

Federal Income Tax – Legislative Changes

Federal income tax provisions have been tweaked frequently since 2001, when EGTRRA reduced marginal tax rates across the board and created a new 10 percent tax bracket carved out of the lower portion of the 15 percent tax bracket. EGTRRA tax provisions were originally scheduled to be phased in over several years, including gradual reduction and ultimate repeal of the estate tax (starting in 2002) and the limits on itemized deductions and personal exemptions (beginning in 2006), with marriage penalty relief beginning in 2005.

The Jobs and Growth Tax Relief Reconciliation Act of 2003 accelerated a number of EGTRRA's personal income tax cuts, including reductions in tax rates and phase-in of marriage penalty relief beginning in 2003. The Act made a number of temporary changes for 2003 and 2004, including increasing the child tax credit to $1,000, increasing the amount of income subject to the new 10 percent tax rate, and increasing the alternative minimum tax exemption. The Act also temporarily (through 2008) reduced to 15 percent the top tax rate imposed on corporate dividends received by individuals after 2002 and on individuals' capital gains realized on or after May 6, 2003.

The Working Families Tax Relief Act of 2004 extended certain tax cuts aimed at middle-class Americans, including: (i) increasing the breakpoint between the 10 percent and 15 percent tax rates through 2010, (ii) increasing the child tax credit to $1,000 through 2009, (iii) accelerating the increase in refundability of the child tax credit to 2004 and including combat pay in earned income for this purpose, (iv) extending marriage penalty relief through 2008 and (v) extending alternative minimum tax relief through 2005. In addition, the Act established a uniform definition of child for purposes of the dependency exemption, child tax credit, earned income credit, dependent care credit and head-of-household filing status.

Table 1

IRS Limit	2005 Unrounded	2005 Rounded	2004	2003	2002
401(k), 403(b), and eligible 457 plan elective deferral limit[1]	$14,000	$14,000	$13,000	$12,000	$11,000
414(v)(2)(B)(i) catch-up contribution limit (plans other than SIMPLE plans)[1]	4,000	4,000	3,000	2,000	1,000
408(p)(2)(E) SIMPLE plan elective deferral limit[1]	10,000	10,000	9,000	8,000	7,000
414(v)(2)(B)(ii) SIMPLE plan catch-up contribution limit[1]	2,000	2,000	1,500	1,000	500
408(k)(2)(C) SEP minimum compensation	480	450	450	450	450
219(b)(1)(A) IRA maximumdeductible amount[1]	4,000	4,000	3,000	3,000	3,000
219(b)(1)(B) IRA catch-up contribution amount[1]	500	500	500	500	500
415(b) defined benefit maximum annuity	170,656	170,000	165,000	160,000	160,000
415(c) defined contribution maximum annual addition	42,664	42,000	41,000	40,000	40,000
401(a)(17) and 408(k)(3)(C) compensation limit	213,320	210,000	205,000	200,000	200,000
401(a)(17) compensation limit for eligible participants in certain governmental plans in effect July 1, 1993	315,120	315,000	305,000	300,000	295,000
414(q)(1)(B) highly compensated employee and 414(q)(1)(C) top-paid group	96,384	95,000	90,000	90,000	90,000
416(i)(1)(A)(i) officer compensation for top-heavy plan key employee definition	138,658	135,000	130,000	130,000	130,000
1.61-21(f)(5) control employee for fringe benefit valuation purposes					
Officer compensation	85,845	85,000	80,000	80,000	80,000
Employee compensation	171,690	170,000	165,000	160,000	160,000
409(o)(1)(C) tax-credit ESOP distribution period					
5-year maximum balance	853,280	850,000	830,000	810,000	800,000
1-year extension	170,656	170,000	165,000	160,000	160,000

[1] 2005 limit is set by statute.

Table 3 on page 7 summarizes the effective dates of key federal income tax changes made by EGTRRA, the Jobs and Growth Tax Relief Reconciliation Act and the Working Families Tax Relief Act. Unless these changes are extended by future legislation, pre-EGTRRA provisions will be restored after 2010.

Federal Income Tax Factors

The breakpoints between tax rates and various other federal income tax factors are adjusted annually on the basis of year-to-year changes in the average CPI-U for the 12 months ending August 31—a 2.3 percent increase, before rounding, for 2005. The IRS published the 2005 rounded limits in Rev. Proc. 2004-71. See Table 4 on page 8.

(continued on page 6)

Table 2

IRS Limit	2005	2004	2003	2002	2001
132(f) tax-free qualified transportation fringe benefit					
Parking	$200	$195	$190	$185	$180
Transit passes or commuter highway vehicle transportation	105	100	100	100	65
137 qualified adoption assistance program					
Exclusion for child with special needs (regardless of expenses incurred)	10,630	10,390	10,160	10,000	6,000
Aggregate limit on expenses incurred for all taxable years (child without special needs)	10,630	10,390	10,160	10,000	5,000
Phase-out begins at adjusted gross income of	159,450	155,860	152,390	150,000	75,000
220(c)(2) MSA high deductible health plan – self-only coverage					
Minimum annual deductible	1,750	1,700	1,700	1,650	1,600
Maximum annual deductible	2,650	2,600	2,500	2,500	2,400
Maximum out-of-pocket limit	3,500	3,450	3,350	3,300	3,200
220(c)(2) MSA high deductible health plan – family coverage					
Minimum annual deductible	3,500	3,450	3,350	3,300	3,200
Maximum annual deductible	5,250	5,150	5,050	4,950	4,800
Maximum out-of-pocket limit	6,450	6,300	6,150	6,050	5,850
223 HSA/HDHP limits – self-only coverage					
Maximum deductible HSA contribution	2,650	2,600			
HDHP minimum annual deductible	1,000	1,000	NA	NA	NA
HDHP maximum out-of-pocket limit	5,100	5,000			
223 HSA/HDHP limits – family coverage					
Maximum deductible HSA contribution	5,250	5,150			
HDHP minimum annual deductible	2,000	2,000	NA	NA	NA
HDHP maximum out-of-pocket limit	10,200	10,000			
213(d) qualified long-term care premium limits					
Age 40 or younger	270	260	250	240	230
41 – 50	510	490	470	450	430
51 – 60	1,020	980	940	900	860
61 – 70	2,720	2,600	2,510	2,390	2,290
Over 70	3,400	3,250	3,130	2,990	2,860
7702B(d)(4) qualified long-term care contract per diem limit	240	230	220	210	200

Personal exemptions are currently phased out for taxpayers whose adjusted gross incomes exceed specified amounts (which vary by tax filing status). These "threshold amounts" at which phase-out begins and ends are shown for 2004 and 2005. EGTRRA reduces the phase out of personal exemptions beginning in 2006 and eliminates it in 2010. See Table 5 on page 8.

Total itemized deductions for 2005 are reduced by 3 percent of a taxpayer's adjusted gross income in excess of $145,950 ($72,975 for married, filing separately), an increase from $142,700 in 2004 ($71,350 for married, filing separately). This reduction in itemized deductions is phased out beginning in 2006 and eliminated in 2010.

Certain taxpayers are entitled to a refundable earned income tax credit (EITC) equal to the maximum credit amount reduced by the phase-out amount. The earned income amount is the amount of earned income at or above which the maximum earned income credit is allowed. The phase-out amount equals the product of the phase-out percentage (based on the number of qualifying children) multiplied by the excess, if any, of the taxpayer's adjusted gross income or earned income, whichever is greater, over the threshold phase-out amount. For tax years beginning after 2001, only taxable earned income (excluding salary reduction contributions under 401(k) plans, cafeteria plans and health or dependent care FSAs) is taken into account when calculating the EITC. EGTRRA marriage penalty relief increased the threshold phase-out amount for joint return filers by $1,000 in 2002–04, by $2,000 in 2005–07, and by $3,000 after 2007. The Working Families Tax Relief Act of 2004 allows taxpayers to optionally include combat pay in earned income for purposes of the EITC for 2004 and 2005. See Table 6 on page 9.

Table 3

Provision	Pre-EGTRRA	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Tax rates	39.6%	39.1%	38.6%	35.0%							
	36.0%	35.5%	35.0%	33.0%							
	31.0%	30.5%	30.0%	28.0%							
	28.0%	27.5%	27.0%	25.0%							
	15.0%	15% for portion of bracket above new 10% breakpoint									
		10% of income up to $6,000 (single)/$12,000 (married) in 2001 and 2002; breakpoints increased to $7,000/$14,000 in 2003 and indexed for inflation thereafter									
Child credit	$500	$600		$1,000							
Saver tax credit	N/A	N/A	Applicable percentage[1] of qualified retirement savings contributions up to $2,000					Expired			
Estate tax Top rate	55%	55%	50%	49%	48%	47%	46%	45%			Repealed
Exemption (millions)	$0.675	$0.675	$1.0		$1.5		$2.0			$3.5	Repealed
Marriage penalty relief beginning in 2003 Standard deduction for married as % of single				200%							
15% of bracket maximum income for married as % of single				200%							
Phase-out of personal exemption and itemized deductions beginning in 2006							Phase-out amount is reduced by 1/3		Phase-out amount is reduced by 2/3		Repealed
Alternative minimum tax exemption Joint return or surviving spouse	$45,000	$49,000		$58,000			$45,000				
Other individual	$33,750	$35,750		$40,250			$33,750				
Top capital gains tax rate	20%			15% (capital gains realized on or after 5/6/03 and before 2009						20%[2]	
Top dividend tax rate	39.6%	39.1%	38.6%	15%						35%	

[1] Saver tax credit applicable percentage is a function of filing status and adjusted gross income (AGI), as shown below:

Applicable percentage	Married filing jointly AGI	Head of household AGI	Other filing status AGI
50%	up to $30,000	up to $22,500	up to $15,000
20%	$30,001-$32,500	$22,501-$24,375	$15,001-$16,250
10%	$32,501-$50,000	$24,376-$37,500	$16,251-$25,000
0%	over $50,000	over $37,500	over $25,000

[2] Once the provisions of the Jobs and Growth Act expire, a top rate of 18% may apply to certain quialified five-year gains.

Social Security and Supplemental Security Income (SSI) Amounts

The Social Security Administration (SSA) announced on October 19, 2004, that benefits will increase 2.7 percent in January 2005. This is the increase in CPI-W from the third quarter of 2003 to the third quarter of 2004. The average monthly Social Security benefits before and after the 2.7 percent COLA are shown in Table 7 on page 9 and in the SSA's fact sheet.

The 2005 taxable wage base will increase 2.4 percent, from $87,900 to $90,000, determined from the change in deemed average annual wages from 2002 to 2003. Table 8 on page 10 shows this and other indexed 2005 and 2004 Social Security and SSI values.

Medicare Premiums, Coinsurance and Deductibles

On September 3, the Department of Health & Human Services announced a 17 percent increase in the Medicare Part B premiums. (The Part B premium increase may not exceed any beneficiary's cost of living adjustment in his or her Social Security check.)

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Table 4

Item and Filing Status	2005	2004
Personal exemption	$3,200	$3,100
Standard deduction		
Single	5,000	4,850
Head of household	7,300	7,150
Married, filing jointly	10,000	9,700
Married, filing separately	5,000	4,850
Additional standard deduction (for elderly or blind)		
Unmarried	1,250	1,200
Married (each)	1,000	950
"Kiddie" deduction	800	800
Breakpoint between 10% and 15% rates[1]		
Single	7,300	7,150
Head of household	10,450	10,200
Married, filing jointly	14,600	14,300
Married, filing separately	7,300	7,150
Breakpoint between 15% and 25% rates		
Single	29,700	29,050
Head of household	39,800	38,900
Married, filing jointly	59,400	58,100
Married, filing separately	29,700	29,050
Estates and trusts (include VEBA trusts)	2,000	1,950
Breakpoint between 25% and 28% rates		
Single	71,950	70,350
Head of household	102,800	100,500
Married, filing jointly	119,950	117,250
Married, filing separately	59,975	58,625
Estates and trusts (include VEBA trusts)	4,700	4,600
Breakpoint between 28% and 33% rates		
Single	150,150	146,750
Head of household	166,450	162,700
Married, filing jointly	182,800	178,650
Married, filing separately	91,400	89,325
Estates and trusts (include VEBA trusts)	7,150	7,000
Breakpoint between 33% and 35% rates		
Single	326,450	319,100
Head of household	326,450	319,100
Married, filing jointly	326,450	319,100
Married, filing separately	163,225	159,550
Estates and trusts (include VEBA trusts)	9,750	9,550

[1] The 10% tax bracket does not apply to estates and trusts.

Table 5

Filing Status	2005		2004	
	Phase-out begins at	Phase-out completed after	Phase-out begins at	Phase-out completed after
Unmarried	$145,950	$268,450	$142,700	$265,200
Head of household	182,450	304,950	178,350	300,850
Married, filing jointly	218,950	341,450	214,050	336,550
Married, filing seperately	109,475	170,725	107,025	168,275

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Table 6

EITC value	2005	2004
Earned income amount		
No qualifying children	$5,220	$5,100
One qualifying child	7,830	7,660
Two or more qualifying children	11,000	10,750
Maximum credit amount		
No qualifying children	399	390
One qualifying child	2,662	2,604
Two or more qualifying children	4,400	4,300
Threshold phase out amount (and percentage), unless married filing jointly		
No qualifying children (7.65%)	6,530	6,390
One qualifying child (15.98%)	14,370	14,040
Two or more qualifying children (21.06%)	14,370	14,040
Phase-out completed, unless married filing jointly		
No qualifying children	11,750	11,490
One qualifying child	31,030	30,338
Two or more qualifying children	35,263	34,458
Threshold phase-out amount (and percentage), married filing jointly		
No qualifying children (7.65%)	8,530	7,390
One qualifying child (15.98%)	16,370	15,040
Two or more qualifying children (21.06%)	16,370	15,040
Phase-out completed, married filing jointly		
No qualifying children (7.65%)	13,750	12,490
One qualifying child (15.98%)	33,030	31,338
Two or more qualifying children (21.06%)	37,263	35,458

Table 7

Average Monthly Social Security Benefit	After 2.7% COLA	Before 2.7% COLA
All retired workers	$955	$930
Aged couple, both receiving benefits	1,574	1,532
Widowed mother and two children	1,979	1,927
Aged widow(er) alone	920	896
Disabled worker, spouse and children	1,497	1,458
All disabled workers	895	871

Table 9 on page 10 shows the increases in premiums, deductibles and coinsurance amounts to be paid by Medicare beneficiaries from 2004 to 2005.

Covered Compensation

For qualified retirement plans, the permitted and imputed disparity limits are based on covered compensation—the average OASDI contribution and benefit base for the 35-year period ending with the year the employee attains Social Security retirement age. In lieu of using the actual covered compensation amount, qualified plans may determine permitted or imputed disparity using a rounded covered compensation table published annually by the IRS. The 2005 table (Table 10 on page 11), published in Rev. Rul. 2004-104, rounds values to the nearest $3,000 (and also shows unrounded values extending back to 1907). The IRS rounds Social Security retirement ages up to the next higher integer for covered compensation purposes, even though the actual Social Security full retirement age increases in two-month increments. ◆

This article was prepared by the Washington Resource Group and the Information Research Center of Mercer Human Resource Consulting. For more information, contact the InfoServices team at 202 263 3950. *Copyright © 2004.*

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Table 8

Social Security/SSI Value		
Cost of living increase	2.7%	2.1%
Average annual wage (second preceding year)	$34,064.95	$33,252.09
OASDI contribution and benefit base (wage base)	90,000	87,900
"Old law" contribution and benefit base	66,900	65,100
Retirement earnings test exempt amount (annual)		
Under full retirement age (full year)	12,000	11,640
Year individual attains full retirement age (period before attaining full retirement age)	31,800	31,080
Wages needed for a quarter of coverage	920	900
Disability thresholds		
Substantial gainful activity—non-blind	830	810
Substantial gainful activity—blind	1,380	1,350
Trial work period	590	580
Coverage thresholds for:		
Domestic employees	1,400	1,400
Election workers	1,200	1,200
Maximum monthly Social Security benefit for a worker retiring at full retirement age (age 65 and 4 months for those born in 1939, age 65 and 6 months for those born in 1940)	1,939	1,825
Bend-points—PIA formula applied to worker's average indexed monthly earnings (AIME)		
90% of AIME up to	627	612
32% of AIME over first bend-point up to	3,779	3,689
15% of AIME over second bend-point	1,508	1,472
Bend-points—Maximum family benefit formula applied to worker's PIA		
150% of PIA up to	801	782
272% of PIA over first bend-point up to	1,156	1,129
134% of PIA over second bend-point up to	1,508	1,472
15% of PIA over third bend-point		
SSI federal payment standard		
Individual	579	564
Couple	869	846
SSI resources limit		
Individual	2,000	2,000
Couple	3,000	3,000
SSI student exclusion limits		
Monthly limit	1,410	1,370
Annual limit	5,670	5,520

Table 9

Part A—Hospital Insurance	2005	2004
Inpatient hospital deductible	$912.00	$876.00
Coinsurance		
Daily coinsurance payment for 61–90 days of inpatient hospital care	228.00	219.00
Coinsurance for up to 60 lifetime reserve days	456.00	438.00
Daily coinsurance payment for 21–100 days in a skilled nursing facility following a hospital stay of at least 3 days	114.00	109.50
Voluntary premium for persons not eligible for monthly benefits	375.00	343.00
Alternative reduced premium for persons with 30–39 credits	206.00	189.00
Part B—Medical Insurance	**2005**	**2004**
Annual deductible	110.00	100.00
Monthly premium	78.20	66.60

Table 10

Calendar year of birth	Social Security full retirement age	Calendar year of Social Security retirement age	Covered compensation		Rounded covered compensation	
			2005	2004	2005	2004
1925	65	1990	18,312	18,312	18,000	18,000
1926	65	1991	19,728	19,728	21,000	21,000
1927	65	1992	21,192	21,192	21,000	21,000
1928	65	1993	22,716	22,716	24,000	24,000
1929	65	1994	24,312	24,312	24,000	24,000
1930	65	1995	25,920	25,920	27,000	27,000
1931	65	1996	27,576	27,576	27,000	27,000
1932	65	1997	29,304	29,304	30,000	30,000
1933	65	1998	31,128	31,128	30,000	30,000
1934	65	1999	33,060	33,060	33,000	33,000
1935	65	2000	35,100	35,100	36,000	36,000
1936	65	2001	37,212	37,212	36,000	36,000
1937	65	2002	39,444	39,444	39,000	39,000
1938	65 & 2 months	2004	43,992	43,992	45,000	45,000
1939	65 & 4 months	2005	46,344	46,284	45,000	45,000
1940	65 & 6 months	2006	48,696	48,576	48,000	48,000
1941	65 & 8 months	2007	51,012	50,832	51,000	51,000
1942	65 & 10 months	2008	53,268	53,028	54,000	54,000
1943	66	2009	55,464	55,164	54,000	54,000
1944	66	2010	57,636	57,276	57,000	57,000
1945	66	2011	59,772	59,352	60,000	60,000
1946	66	2012	61,872	61,392	63,000	60,000
1947	66	2013	63,936	63,396	63,000	63,000
1948	66	2014	65,856	65,256	66,000	66,000
1949	66	2015	67,680	67,020	69,000	66,000
1950	66	2016	69,408	68,688	69,000	69,000
1951	66	2017	71,052	70,272	72,000	69,000
1952	66	2018	72,600	71,760	72,000	72,000
1953	66	2019	74,100	73,200	75,000	72,000
1954	66	2020	75,540	74,580	75,000	75,000
1955	66 & 2 months	2022	78,228	77,148	78,000	78,000
1956	66 & 4 months	2023	79,512	78,372	81,000	78,000
1957	66 & 6 months	2024	80,712	79,512	81,000	81,000
1958	66 & 8 months	2025	81,816	80,556	81,000	81,000
1959	66 & 10 months	2026	82,860	81,540	84,000	81,000
1960	67	2027	83,844	82,464	84,000	81,000
1961	67	2028	84,780	83,340	84,000	84,000
1962	67	2029	85,620	84,120	87,000	84,000
1963	67	2030	86,436	84,876	87,000	84,000
1964	67	2031	87,216	85,596	87,000	87,000
1965	67	2032	87,924	86,244	87,000	87,000
1966	67	2033	88,536	86,796	90,000	87,000
1967	67	2034	89,040	87,240	90,000	87,000
1968	67	2035	89,424	87,564	90,000	87,900
1969	67	2036	89,700	87,780	90,000	87,900
1970	67	2037	89,844	87,864	90,000	87,900
1971	67	2038	89,940	87,900	90,000	87,900
1972 or later	67	2039 or later	90,000	87,900	90,000	87,900

Retirement Probability Analyzer Software Released

Wall Street Journal Article Touts its Merits

by Emily K. Kessler

The SOA recently released the Retirement Probability Analyzer Software, which can be downloaded at no charge from its Web site. Finance Professor Moshe Milevsky of York University (Ontario) and his team at the IFID Centre created the software. The software provides a unique way to analyze the probability of financial ruin during retirement. The software was sponsored by the Pension Section to develop a practical application of theoretical work by Dr. Milevsky on ways to use annuitization to optimize financial security in retirement.

The software differs from others currently available in the mathematical analysis it uses to determine the probability of a successful financial strategy and in its ability to illustrate longevity risks. Most retirement financial planning software uses Monte Carlo simulations of the portfolio to determine the probability that the financial strategy will be successful, and generally only look at life expectancy, or a single set age, in assigning those probabilities. The Retirement Probability Analyzer uses a numerical procedure based on partial differential equations in its analysis. The resulting projections, therefore, do not contain statistical sampling error. Also, it is able to project probabilities of ruin looking at four future time periods—10 years, 20 years, 30 years and lifetime.

The tool includes inputs typical to similar models: asset allocation, economic assumptions and individual information.

The tool specifically factors in the power of annuities to protect against financial ruin. It allows a user to model changes in the mix of lifetime income and lump sum investable wealth and the interaction of those changes with market and longevity risk. The tool includes inputs typical to similar models: asset allocation, economic assumptions and individual information. It also includes factors not usually found in such tools but important to actuaries, such as mortality projections and assumptions for annuity valuation rates. Output items include:

- The probability that an individual's nest egg—the net investable wealth (NIW)—is some fraction of the initial NIW within a future time period (10 years, 20 years, 30 years or lifetime).
- Projected wealth (conditional on survival) in 10, 20 or 30 years.
- Projected consumption, showing changes in consumption as the NIW is depleted.
- Risk of the current strategy vis-à-vis expected lifetime (expected age at ruin and the probability of survival beyond that age).

The Retirement Probability Analyzer was the focus of a *Wall Street Journal* article on page 31 of the August 2004 edition. The article, "Tool Tells How Long Next Egg Will Last," noted the Retirement Probability Analyzer as a tool for "people who want their projections to be a bit more sophisticated than those offered by most online calculators." The article looked at the tool in light of other free software available to individuals for calculation purposes. Because the program was designed as an educational tool for a sophisticated financial professional, it does not have the slick appearance or extensive help features of other software. But, as noted, "what [it] lacks in appearance, it makes up for in content." The article acknowledged the strength the tool brings to the analysis of the balance between invested assets and annuitization.

The Retirement Probability Analyzer and accompanying documentation can be found on the SOA Web site at *http://www.soa.org/ccm/content/areas-of-practice/special-interest-sections/pension/retirement-probability-analyzer-software/.* An excerpt of the *Wall Street Journal* article is available on the SOA Web site at *http://www.soa.org/ccm/content/areas-of-practice/ special-interest sections/pension/retirement-planning-calculating-risk-of-retirement-woes/.* ◆

Emily K. Kessler, FSA, MAAA, is an SOA staff fellow, retirement systems. She can be reached at ekessler@ soa.org.

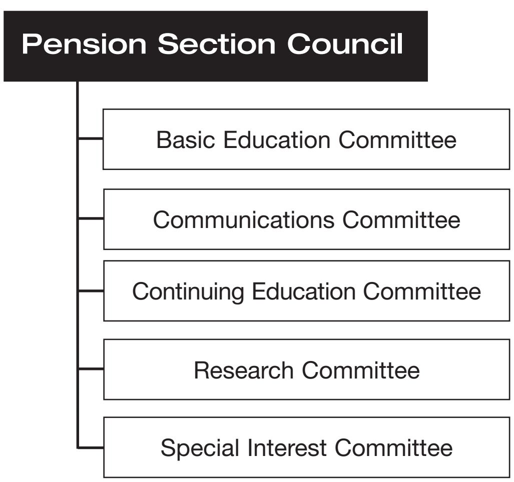
New Structure of the Section Council

by Emily K. Kessler

Okay, we hate talking about ourselves and how we're organized. But periodically it must be done, particularly when everything is changing. So, without further apologies …

The Pension Section has taken on additional responsibilities as the SOA continues its reorganization of sections and practice areas. Not sure what a practice area is and what it means to reorganize sections and practice areas? Don't worry about it. Even if you do know what a practice area is (or was), all you need to know now is what's going on in the future, where to get information and how to get involved.

The Pension Section has taken on additional responsibilities in the new structure. Some of what the Section Council is doing are things they've done before, on an ad-hoc basis, and some are new to the Section Council. To help the Section Council get its work done, it is going to organize itself as follows:



The Section Council will take on new responsibilities, including areas such as:

- Environmental scanning: Identifying and communicating current, emerging and potential issues, topics and trends relevant to the section's members.
- Communicating with the Board of Governors. As your connection to the Board of Governors, the Section Council will be more closely communicating what it's doing and learning about what the Board of Governors is working on.
- Taking responsibility for the identification and prioritization of experience studies and ensuring they are properly executed and meet members' needs.
- Leveraging the section's connections to further strategic initiatives of the SOA.
- Advocating for the interests and needs of pension actuaries outside the SOA (but not in ways that conflict with other actuarial organizations (e.g., the CIA, Academy).
- Establishing and maintaining external relationships with other non-actuarial organizations to enhance opportunities and increase visibility for the profession and professional development (but not in ways that conflict with other actuarial organizations (e.g., the CIA, Academy).
- Provide thought leadership for the pension actuarial community.

Many of these duties are new to the Section Council, and as such they saw the need to establish a new structure to ensure their other responsibilities are completed. These subcommittees are new to the Section Council; many of them are coming directly from the old Retirement Systems Practice Area committees, some are brand new.

1) **Basic Education Committee.** This is a new committee, and a new opportunity for section members to get involved in influencing the basic education process (also known as the examination system). The committee will be charged with:

   – Providing input on basic education content.
   – Answering requests from SOA basic education committees (e.g., for help writing study notes).
   – Providing regular review of the basic education syllabus.
   – Providing an avenue for the pension actuarial community's input to basic education process.

(continued on page 14)

The Pension Section has taken on additional responsibilities as the SOA continues its reorganization of sections and practice areas.

Above: Attending the October Pension Section Concil Meeting were outgoing co-chair, Ian Genno, Ken Kent and outgoing co-chair Susan Wright.

Note: This committee has a different function from the Education & Examination Committees. It has no direct responsibility for syllabus planning or writing the exams. Its role instead is to act as an advisor and to help ensure that the syllabus includes the right material for pension actuaries.

2) **Communications Committee.** This is also a new committee, but an existing function of the Section Council. The council decided to move responsibilty to a new group as it takes on additional responsibiities, but also to renew a focus. This committee will be charged with:

– Publicizing issues of interest to practitioners. This includes finding out what other associations and professional groups with similar interests are doing, and making sure news of their activities is communicated to section members.
– Overseeing responsibility for *Pension Section News,* the *Pension Forum*, and the Pension Section's Web site.
– Provide input to *The Actuary*.

While this is a new group, it already has one hardworking member, our current Pension Section News editor, Art Assantes.

3) **Continuing Education Committee.** Under the prior structure, there were two groups who worked on continuing education needs for retirement practitioners: The Committee for Retirement Systems Professional Education & Development (CRSPED) and the Pension Section Council. Now, the responsibility will lie with one group, the Section Council's Continuing Education Committee. We've asked members of CRSPED to step over and continue their work under the Section Council. This committee is charged with identifying and developing content for continuing education. It's a one-sentence mission statement that covers a lot, including the spring and annual meetings, webcasts, seminars and symposiums. In 2004, through the efforts of the Section Council and CRSPED 16 sessions for the spring meeting and14 sessions for the annual meeting (which includes the Brave New World Financial Economics Seminar) were held. In addition, a series of four webcasts were held in the fall.

4) **Research Committee.** Again, under the prior structure, there were two groups participating in research activities: The Committee for Retirement Systems Research (CRSR) and the Pension Section Council. Once again, the work of these two groups will be folded into one committee, the Section Council's Research Committee. And once again, we've asked members of CRSR to step over and continue their work under the Section Council. It's another one-sentence mission statement that encom passes a lot: identifying and overseeing research initiatives. In 2004, the efforts of the Section Council and CRSR resulted in the completion of a turnover study and release of the Retirement Probability Analyzer software. A paper on Corporate Bond Yields (coming in the Pension Forum in the 4th quarter) was commissioned and a cash balance plan survey (for completion in 4th quarter 2004/1st quarter 2005) was started. And there are many more projects in the development stages.

5) **Special Interest Committees**. These are three committees that have existed under the practice area, which will be moved under the Pension Section Council. They are:

– *Committee on Post-Retirement Needs and Risks.* This group focuses on the issue of risks faced by individuals after retirement—what do we know about them and how to manage and/or mitigate them—and what can be done to educate the public and practitioners about those risks. Chaired by Anna Rappaport, this group has a membership far outside the actuarial profession, including interested parties from the AARP, EBRI, LIMRA, NASI, WISER and various universities. The group has been very busy and published the 2003 Risks and Process of Retirement Survey, two short reports on the Risks and Process of Retirement and the up coming paper on Public Misperceptions of Retirement.

– *Joint Academy/Society Task Force on Financial Economics and the Actuarial Model.* This is the group responsible for the Vancouver symposium (2003) and the webcast series (2003/2004). Its mission is to determine if and then how financial economic principles might be incorporated into pension actuarial practice. It continues its work, including content for a spring seminar, a roundtable discussion and Web page.

– *Committee on Social Security.* This group is charged with looking at actuarial issues facing social insurance systems, particularly those in the United States and Canada. It doesn't advocate for change (that's the CIA/Academy role); instead it focuses on deriving a better understanding of the technical issues facing the systems.

Each of these groups is filled with volunteers with a passion for what they do. Working on a volunteer committee can help you expand your horizons and become a better pension practitioner. If you're interested in joining, contact Emily Kessler at *ekessler@soa.org* to learn more about what you can do. ◆

Hot off the press!

Life Insurance and Modified Endowments Under Internal Revenue Code Sections 7702 and 7702A

Get your copy of the Society of Actuaries' newest publication and first-ever book on this topic. This innovative work provides a practical look at the issues surrounding federal income tax treatment of life insurance contracts, including in-depth information on the statutory definition of life insurance found in Section 7702 of the Internal Revenue Code and the modified endowment rules in Section 7702A.

Leading experts in the field, actuaries Chris DesRochers, Doug Hertz and Brian King teamed up with attorney John Adney to author a well-balanced book, combining their extensive knowledge.

For more information or to order a copy, please visit the SOA Web site at *http://books.soa.org*.

Pension Section Council Summary of Activities

by Anne M. Button

Note: This summary of activities was written in October 2004. Many activities referred to as future events/projects will have been held/completed.

The Pension Section Council had meetings via conference calls in July, August, September and early October, and attended a joint meeting in September with members of the Retirement Systems Practice Advancement Committee. Following is a summary of the current activities of the Pension Section Council.

The council is continuing to explore the feasibility of developing and supporting a Web site that would provide understandable information to the general public on issues relating to retirement income delivery and security.

Research Projects

Projects that the Pension Section is currently supporting include:

- The voluntary annuitization project by Moshe Milevsky has been completed and the software tool that examines the financial issues faced by individuals when they convert lump sum retirement savings balances into ongoing income streams is now available on the Web site and has received favorable press coverage.
- A project on preretirement influences by Linda Smith-Brothers, which involves a literature search to explore the various factors that influence an employee's decision to retire. The project has been expanded due to the large universe of articles related to this subject. The first phase of this project will be completed by the end of 2004.
- Retirement rate assumptions: focus on developing methodology and guidance as well as sensitivity analysis.
- Phased retirement: provide assistance to the project oversight group that is being established by the Research Committee.
- Solving the portability problem—a call for papers will be issued shortly.
- Articulating how a "rational" retirement age should be developed.
- Long-term implications of retirees lacking post-retirement medical coverage.

The council is always interested in ideas for practical research, so please contact a member of the council if you have suggestions.

Pension Forum

There are two forums that are still on target to be completed in 2004 and early 2005:

- One forum will focus on the yield curve, including one paper on how yield curves are developed and two papers discussing how yield curves may be used in valuing pension liabilities.
- The other forum will center around the paper, "A Re-evaluation of ASOP 27, Post-Enron: Is It An Adequate Standard of Professionalism?" by Frank Todisco and include additional papers in response to Frank's paper.

A forum with articles from the Vancouver Financial Economics Symposium is expected to be published later in 2005.

Statistics for Employee Benefits Actuaries

The statistics have been posted to a separate password protected Web site that is available only to Pension Section members. Please contact the SOA if you are a member and have lost the link and/or password.

Webcasts

The council has sponsored three webcasts regarding pensions and OPEB this fall. The first two webcasts were held in September: the first on the "Relative Value Regulations" and the second on "Accounting for Medicare Part D." The third webcast, "Pension and OPEB Accounting Trends: What Next?" will be held November 16.

Spring Meeting

The council proposes to change how the pension-related portion of the SOA spring meeting is structured. Rather than offer a cafeteria-style selection of 1 1/2 hour sessions on various topics, we will focus on developing one or two in-depth seminars examining specific topics for the 2005 spring meeting. The subject of the seminar(s) will be confirmed at our next meeting scheduled for October 28.

Retirement Information Web Site

The council is continuing to explore the feasibility of developing and supporting a Web site that would provide understandable information to the general public on issues relating to retirement income delivery and security. Information that may be provided would include education regarding the various approaches to providing retirement income and the various risks inherent with making decisions about retirement including considerations in selecting assumptions, the time value of money, the risk of outliving assets, etc.

SOA Governance

Several members of the council are continuing to participate in ongoing discussions within the Society regarding the governance review and the future organizational structure that will most efficiently meet members' needs. This was the focus of the September meeting with RSPAC.

Living to 100 Symposium

The council voted to provide $7,500 in funding to support this symposium. The research included in this symposium could affect the calculation of pension liabilities.

New Council Members

The council welcomed Josh Bank of Deloitte Consulting LLP, Tammy Dixon of The Segal Company

Right: Pension Section Council Members met in New York after the Annual Meeting. Pictured from left to right are: Joshua Banks, Martina Sohier, Ken Kent, Anne Button, Ian Genno, Sarah Wright, Eric Freden, Tonya Manning and Mike Pisula. Not pictured: Betsey Byrd, Art Conat and Tammy Dixon.

and Martine Sohier of Watson Wyatt Worldwide following the SOA elections in August.

Finances

The available funds of the Pension Section are as follows:

Assets as of March 31, 2004	$189,000
Income	**14,000**
Expenses	
Ongoing Functions	1,000
Ongoing Services to Members	23,000
Assets as of June 30, 2004	$179,000

Membership

There were 3,948 members as of April 2004. ◆

Anne M. Button, FSA, MAAA, EA, is senior manager at Deloitte & Touche LLP. She can be reached at 617-437-2171 or anbutton@deloitte.com.

Bad for plan sponsor in the long run
Although the investment risk is in the participant's hands, the employer is also vulnerable. When the market turns down, the employer will suffer from low employee morale as DC assets deteriorate. At the same time, the plan sponsor might want to reduce staff. But with low account values, individuals eligible for retirement will be reluctant to leave, keeping payroll costs high. In addition, without a fully funded DB plan, the employer will not have the tools and the spare cash needed to encourage departures through an early retirement window.

Also, when the economy is good, the plan sponsor might want to increase staff. But at the same time, current employees might see sufficient DC funds for them to retire. Not only will the plan sponsor be pressed to hire new employees to meet growing demands, but he will also need to replace retiring employees.

Bad for society in the long run
As participants make bad savings and investment decisions, they will be left without the means to pay for their retirement. Then society (e.g., taxpayers) will need to make up part if not all of this difference.

Move Assets to Bonds

A better alternative would be to make less risky investments in the DB plans.

Good for shareholder value
Over time, the lower anticipated returns from bonds compared to equities would be expected to raise contribution levels. However, financial economics argues that this increases shareholder value and has socially desirable effects. The benefit to shareholders can be determined by considering the entire portfolio of investments of the shareholders and the tax advantages to investing inside a qualified plan and the tax advantages of investing in equities.

Each shareholder has a certain level of risk that is optimal for him. He achieves this level by dividing his portfolio appropriately between equities and bonds. He prefers to hold his highly taxed assets—bonds—in the tax shelter of a corporate pension plan, and his lower taxed assets—equities—in unsheltered accounts.

Good for participants
When the economy turns down, some employers will close their doors. As employees lose their jobs with this employer, the blow is cushioned by the knowledge that their pensions have not dropped in value as well, and their ability to finance their retirement is unimpaired.

Good for society
As the pension plan fulfills its promises, the retiree population is more financially secure. Therefore, there is likely to be little or no need for social benefits to replace the loss of employee pensions.

Conclusion

Defined benefit plan sponsors have recently suffered from the asset liability mismatch risk. To address this, plan sponsors can make the liabilities (benefits) more like the assets or make the assets more like the liabilities. They can move to defined contribution plans, thereby making benefits like risky assets. A better option is to reduce risk taken by using more secure assets to make assets more like the secure benefits (liabilities). ◆

Pension Section News

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2004-2005 SECTION LEADERSHIP
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Anne M. Button, Vice-Chairperson
Martine Sohier, Secretary
Joshua David Bank, Treasurer
Elizabeth S. Byrd, Council Member
Arthur L. Conat, Council Member
Tammy F. Dixon, Council Member
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Articles Needed for the *News*

Your participation is needed and welcomed. All articles will include a byline to give you full credit for your effort. *Pension Section News* is pleased to publish articles in a second language if a translation is provided by the author. For those of you interested in working on the *Pension Section NewsNews*, several associate editors are needed to handle various specialty areas such as meetings, seminars, symposia, continuing education meetings, teleconferences and cassettes (audio and video) for enrolled actuaries, new pension study notes, new research and studies by Society committees, etc. If you would like to submit an article or be an associate editor, please call Arthur Assantes, editor, at (860) 521-8400.

As in the past, full papers will be published in *The Pension Forum* format, but now only on an ad-hoc basis.

Preferred Format

In order to efficiently handle articles, please use the following format when submitting articles: Please e-mail your articles as attachments in either MS Word (.doc) or Simple Text (.txt) files. We are able to convert most PC-compatible software packages. Headlines are typed upper and lower case. Please use a 10-point Times New Roman font for the body text. Carriage returns are put in only at the end of paragraphs. The right-hand margin is not justified.

If you must submit articles in another manner, please call Erica Barraca, (847) 706-3549, at the Society of Actuaries for assistance.

Please send a hard copy of the article to:
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SOA Seminar:

Addressing the Financial Risks from Retirement Systems

Thirty years ago, defined benefit plans were relatively smaller in relationship to the plan sponsor's core business or sponsoring government's infrastructure. A graying baby boom population, increased longevity and contraction of old-line industries have combined to increase the cost and financial risk engendered by pension plans. Once small fringe benefits, retirement plans have become substantial financial commitments with the accompanying risk. Many plan sponsors have reacted by terminating or freezing plans and moving to defined contribution plans.

Actuaries must help plan sponsors get back to the basics: the costs and risks inherent in defined benefit and defined contribution plans before the accumulated overlay of regulation. To help in this process, the Pension Section Council's Continuing Education Committee has designed this two-day intensive seminar and embedded it into the SOA Health/Pension Spring Meeting. The goal of the seminar is to help you better measure, discuss, manage and mitigate risks that pension plans bring to their sponsoring organizations.

Go to *http://www.soa.org/ccm/content/?categoryID=344002* for more details. If you're interested in participating as a speaker or moderator, contact Emily Kessler at *ekessler@soa.org*. ◆

Save the Date!

2005 SOA Health/
Pension Spring Meeting:
June 16-18, 2005,
New Orleans, LA

SOA/LIMRA/LOMA Retirement and Annuity Conferences and Retirement Symposium

April 6-8, 2005
Westin La Cantera Resort
San Antonio, Texas
For registration information go to: *www.loma.org.*

Employee Benefits Update for 2005

Cosponor with the ABA

Teleconference and Live Audio Webcast
Tuesday February 15, 2005
12:00-4:00pm Eastern
Link to here:
www.abanet.org/cle/programs/nosearch/sebumo.html