

So Many Trails, So Little Time

BY JOHN PARKS

THE T-SHIRT CONTAINING THOSE WORDS shows a solitary backpacker meandering through an enchanting but challenging mountain forest trail. In our 78 million acres of national forests there are thousands of wilderness trails that slink along quiet streams, wander gracefully through meadows, and carve their way, with redundant switchbacks, through mountainsides and avalanche chutes. Hikers confront everything from an easy stroll to a technical three-point climb up a cliff cascading with spring snowmelt. With all of these trails, lingering around every bend or hiding just beyond the next peak are endless beauty, a fearsome obstacle, and, of course, a new trail to be followed.

My two-year term as vice president of the Academy's Pension Practice Council has been somewhat similar—a wonderful experience marked by constant and continuing challenge. Coinciding with the beginning of my term was the Treasury Department's announcement that it was suspending issuance of all new 30-year bonds—a move that galvanized action on finding a replacement benchmark for defined benefit (DB) pension plan calculations. As I prepare to end my term in office, the Bush



administration has announced a new proposal for that replacement rate. Legislative movement on pension reform also continues, with the next generation of Portman-Cardin legislation making its way through Congress. To compare the provisions of current pension reform proposals, see the chart on Page 4. In my view, the Bush proposal is a reasonable beginning, but the end of the trail is not yet in sight. Still

lingering, for instance, are the endless code complexities challenging DB plans in general. While the 30-year Treasury rate and general pension reform measures have claimed a large portion of the council's attention these past two years, there have been other challenges as well.

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A Closer Look at the Bush Savings Proposals

EARLIER THIS YEAR, the Bush administration proposed a major policy initiative intended to promote retirement savings through the establishment of three new types of savings accounts: lifetime savings accounts (LSAs), retirement savings accounts (RSAs), and a consolidated account for 401(k)s, 403(b)s, and 457 plans called employer retirement savings accounts (ERSAs).

These accounts would be funded with after-tax contributions, and earnings would accumulate on a tax-free basis. Withdrawals could be made from the LSA account without

penalty at any time for any purpose; however, withdrawals from the other two types of accounts (RSAs and ERSAs) could only be made without penalty under certain circumstances.

A general overview of the proposals was published in the Spring 2003 *EAR* and is available online at www.actuary.org/ear/pdf/spring_2003.pdf.

What follows is a more detailed analysis prepared by the Academy's Pension Committee for distribution to legislative and regulatory audiences.

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Changing Discount Rates for Determining Lump Sums

Editor's Note: The following is an extract from an analysis written by Ron Gebhardtsbauer, the Academy's senior pension fellow, and Don Segal, chairperson of the Academy's Pension Committee. The complete paper, published by the Pension Committee in June, is available on the Academy's website at www.actuary.org/pdf/pension/discount_061703.pdf.

THE MINIMUM LUMP SUM payable from a pension plan has increased dramatically due to the unusually low 30-year Treasury rates of the past few years. This has made pension plans that have lump-sum provisions much more expensive than the plan sponsor ever intended. Proposals to increase the lump-sum interest rate could reduce lump sums unless they provide a transition period.

PROBLEMS WITH USING THE LOW 30-YEAR TREASURY RATE

As discussed in our testimony (available online at www.actuary.org/testimony.htm#4) before House Ways & Means on April 30, here are several concerns caused by using the unusually low 30-year Treasury rate. For example:

► **SPOUSAL BENEFITS** –The use of Treasury rates for determining lump sums makes the lump-sum amount so large that it discourages employees from taking the plan's automatic joint and survivor annuity. This conflicts with the original intent of ERISA:

to encourage pensions for surviving spouses.

► **PUBLIC POLICY** –Taking lump sums may be viewed negatively from a public policy perspective because more retirees will spend down their lump sum too quickly and end up relying on government assistance (Supplemental Security Income and Medicaid).

► **PLANS FUNDING LEVELS** –The payment of a lump sum from an underfunded plan decreases the funding ratio, particularly if the lump sum is subsidized by the unusually low Treasury rate. In addition, plans will tend to be less well funded, because Notice 90-11 prohibits the subsidy from being included in the current liability calculation. This is a concern not only for participants but also for the PBGC.

► **INCREASED COSTS BEYOND AMOUNTS INTENDED** –Plan sponsors have to contribute more funds to the plan because the low Treasury rate makes lump sums larger (not because the employer decided to increase lump sums). Thus, the plan is more expensive than the employer originally intended.

► **OBSTRUCTION OF COLLECTIVE BARGAINING PROCESS** –Due to the expense of paying larger lump sums, plan sponsors are less able to make plan improvements suggested by workers at the next bargaining period. Thus, requiring the Treasury rate supplants the collective bargaining process and discriminates against participants that don't take lump sums. If employees were permitted to decide where the funds should go, labor organization staff have stated, employees would probably bargain to use the funds



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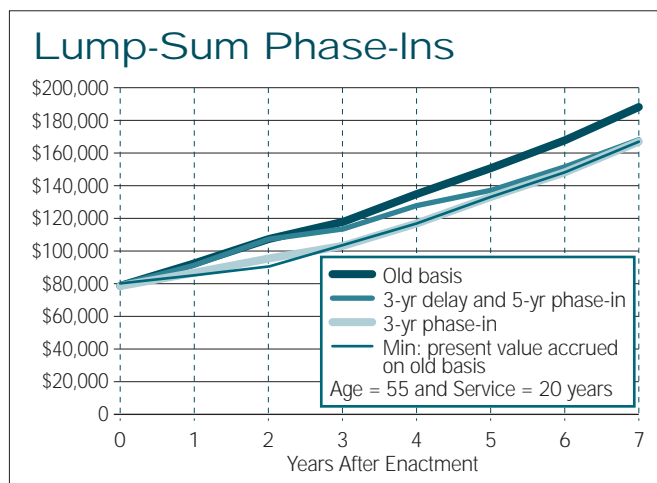
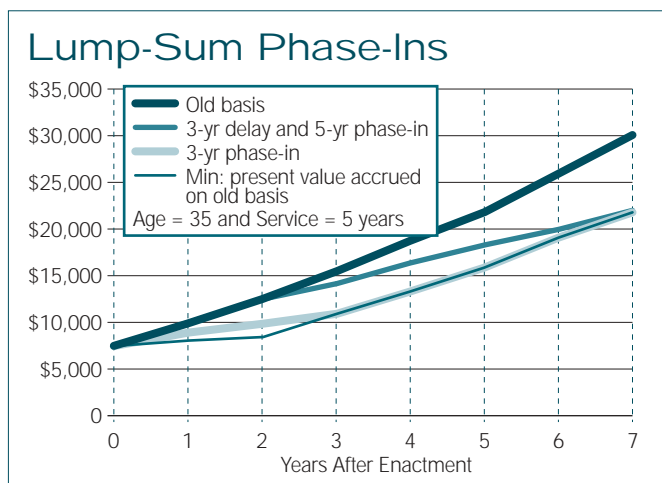
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These charts show the effects of three different transition rules (the ERISA Industry Committee's three-year phase-in, Portman-Cardin's delayed five-year phase-in, and the current anti-cutback rule) on the lump-sum amount. The charts assume that interest rates will remain where they are today. If interest rates go up or down, that will push all of the lump-sum amounts proportionately. The calculations also assume that the new rate is a composite corporate bond rate equal to the average of the high-quality long-term-bond indices of Merrill Lynch, Saloman, Moody's, and Lehman—a rate that is now about 100 basis points higher than the 30-year Treasury rate.

to improve the benefit formula for all workers, as opposed to those who just take lump sums.

TRANSITION RULES

Changing to a higher interest rate can reduce a worker's lump sum, so a transition rule may be helpful. For example, some organizations suggest gradually changing to a composite corporate bond rate over three years. This three-year phase-in could limit the increase in the interest rate to about 34 basis points per year (unless all interest rates rise dramatically in the next three years).

We note that Treasury rates have increased in the past. In 1996 and 1999, the rate went up 150 basis points, so this would not be the first time participants have experienced an increase in lump-sum interest rates. In legislation introduced by Reps. Rob Portman (R-Ohio) and Benjamin Cardin (D-Md.), the transition is delayed three years and then phased in over five years. The delay protects near-term retirees from any change in the lump-sum amount. Furthermore, with a three- or five-year transition, a worker's lump sum will not go down. It will grow because each year workers get additional service and pay increases, and their age gets one year closer to their normal retirement date. In fact, our calculations show that transition rules would keep lump sums from decreasing even if the worker does not receive a pay increase or if the worker's service is greater than the plan maximum. Lump sums can go down, however, for younger employees who had quit employment in the past but had not taken their lump sum. Thus, we would recommend that employers notify them of the change and allow them to cash out before the change takes effect.

MAXIMUM LUMP SUMS

In addition, we suggest Congress simplify the very complex calculations caused by §415(b)(2)(E) for maximum lump sums. One simple alternative suggested by the American Society of

Pension Actuaries would be to use just one interest rate. Our paper, *Alternatives to the 30-Year Treasury Rate* (available at www.actuary.org/pdf/pension/rate_17july02.pdf), suggested that it could be somewhere in the 5 to 8 percent range. The Academy has also suggested to the Treasury Department in the past that the rules could be greatly simplified by deleting the words "or the rate specified in the plan" in §415(b)(2)(E), so that the maximum lump sum would be the same in all plans (and the discount rate used above and below the normal retirement age would be the same). ▲

Pension Stats

THE PBGC HAS ISSUED AN UPDATED VERSION of its annual statistical reference book, the *Pension Insurance Data Book 2002*, which tracks the experience of PBGC's multiemployer and single-employer insurance programs and the defined benefit pension plans they protect.

The book contains graphs and tables on the financial condition of the PBGC's programs, the numbers of people and plans protected by those programs, people receiving or eligible to receive benefits from PBGC—and the benefits paid to them, along with claims against the programs.

The book is available on the PBGC website at www.pb.gc.gov. Single copies may be obtained by writing to: PBGC Data Book, Suite 240, 1200 K Street, N.W., Washington, D.C. 20005-4026. Requests may also be submitted by fax to 202-326-4042.

Proposed Pension Rate Reforms

As the debate continues on pension interest rate replacement, it's getting harder and harder to tell the players without a scorecard. Expect deliberations on the issue to heat up as legislators return to Washington after the August recess.

Issue	Current Law	H.R. 1776—Pension Preservation and Savings Expansion Act (as passed by House Ways and Means Subcommittee) <i>Introduced by Reps. Portman (R-Ohio) and Cardin (D-Md.)</i>	S. 1550—Pension Stability Act <i>Introduced by Sen. Gregg (R-N.H.)</i>
30-year Treasury replacement rate	<p>Current liability interest rate:</p> <ul style="list-style-type: none"> ▶ 2002–2003—upper limit increased to 120% of weighted average of 30-year Treasury rate ▶ 2004 and beyond—upper limit returns to 105% of weighted average of 30-year Treasury rate <p>PBGC variable premium interest rate:</p> <ul style="list-style-type: none"> ▶ 2002–2003—100% of 30-year Treasury rate ▶ 2004 and beyond—85% of 30-year Treasury rate <p>Lump-sum distributions:</p> <ul style="list-style-type: none"> ▶ 2003—30-year Treasury rate ▶ 2004 and beyond—30-year Treasury rate 	<p>Current liability and PBGC variable premium interest rates:</p> <ul style="list-style-type: none"> ▶ 2004–2006 corporate bond rate* ▶ 2007 and beyond—30-year Treasury rate <p>Lump-sum distributions:</p> <ul style="list-style-type: none"> ▶ 2004–2005—30-year Treasury rate ▶ 2006—the lower of corporate bond rate or 30-year Treasury rate plus 20% of the excess of the rate based on the corporate bond rate over the 30-year Treasury rate <p>*Conservatively invested, long-term corporate bond rate determined by the secretary of the Treasury</p>	<p>Current liability interest rate:</p> <ul style="list-style-type: none"> ▶ 2004–2005—maximum composite corporate bond rate ▶ 2005–2008—maximum composite corporate bond rate ▶ 2009 and beyond—30-year Treasury rate <p>PBGC variable premium interest rate:</p> <ul style="list-style-type: none"> ▶ 2004–2008—composite corporate bond rate ▶ 2009 and beyond—30-year Treasury rate <p>Lump-sum distributions:</p> <ul style="list-style-type: none"> ▶ 2004–2005—30-year Treasury rate ▶ 2006—lower of composite corporate bond rate or 30-year Treasury rate plus 20% of the excess of the corporate bond rate over the 30-year Treasury rate ▶ 2007—lower of composite corporate bond rate or 30-year Treasury rate plus 40% of the excess of the corporate bond rate over the 30-year Treasury rate ▶ 2008—lower of composite corporate bond rate or 30-year Treasury rate plus 60% of the excess of the corporate bond rate over the 30-year Treasury rate <p>*Composite corporate bond rate determined by the secretary of the Treasury</p>
Pre-tax employee contributions to DB plans	Employee contributions to DB plan are made on an after-tax basis, except for certain governmental plans.	For plans with qualified mandatory employee contributions as of Jan. 1, 2003, that do not exceed 2% of compensation, employee contributions can be made on a pre-tax basis.	NA
Minimum required distribution age	<p>In general, an individual must begin taking distributions from qualified retirement plans and IRAs on April 1 of the calendar year following the later of the calendar year in which the participant attains 70½ or retires.</p> <p>The penalty for not complying with the minimum required distribution rules is an excise tax of 50% on the amount not distributed.</p>	<p>The age for minimum required distributions is gradually increased as follows:</p> <ul style="list-style-type: none"> ▶ 2004–2007—age 72 ▶ 2008—age 75 <p>The penalty for not complying with the minimum required distribution rules is an excise tax of 20% on the amount not distributed.</p>	NA
Exclusion of percentage of lifetime annuity payments	Distributions from qualified retirement plans and employer-sponsored retirement plans, as well as withdrawals from IRAs, are taxed as ordinary income.	<p>Participants could exclude a portion of retirement annuity income from taxes for the first five years of defined contribution plan annuity payments, limited to the first 10% of annuity payments received during the year and not greater than \$2,000 in 2004.</p> <p>The provision does not include annuity income from DB plans.</p>	NA

record. So we created a scorecard.

Act	Administration Proposal
ridor is ond rate ridor is ond rate Treasury	<p>Current liability interest rate:</p> <ul style="list-style-type: none"> ► 2004–2005—corporate bond rate ► 2006—blend of corporate bond rate and yield curve (weighted 2/3 to 1/3) ► 2007—blend of corporate bond rate and yield curve (weighted 1/3 to 2/3) ► 2008—yield curve <p>Lump-sum distributions:</p> <ul style="list-style-type: none"> ► 2004–2005—30-year Treasury rate ► 2006—blend of corporate bond rate and yield curve (weighted 2/3 to 1/3) ► 2007—blend of corporate bond rate and yield curve (weighted 1/3 to 2/3) ► 2008—yield curve
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SO MANY TRAILS, SO LITTLE TIME *continued from Page 1*

Earlier this year, the administration floated a proposal to establish two new savings vehicles, as well as to consolidate 401(k), 403(b), and 457(b) plans into one account (for the Academy's analysis of these proposals, see Page 1). While the savings plans initially met with resistance among policy-makers, renewed efforts by the administration to encourage these accounts as a means of promoting retirement security means they will not be fading from congressional consciousness.

Trekking beyond the Washington beltway, it is increasingly clear that the problems pension actuaries face are international in scope. Declining fertility rates and increasing life expectancy are challenging the retirement systems (both public and private) of countries throughout the world. In a June symposium sponsored by the Society of Actuaries and the Academy, debate centered on current actuarial models for DB plans in light of financial economics in the United States and other countries. With advocates on both sides of the investment and asset-smoothing issue, this is a debate that the actuarial profession must continue to monitor and analyze.

Looking to future directions, there has been considerable discussion over the past two years on the issue of lump-sum distributions in DB plans. There are two reasons why I strongly believe that lump sums should be disallowed. First, they drain plan assets through an accelerated cash stream at an interest rate considerably lower than the plan's funding rates. More important, they create a culture of planned poverty. Retirees are too easily lured by a large sum of money that quickly dissipates. The logic often heard is that the retiring participant looks at his or her life expectancy as the appropriate endpoint for financial planning purposes. However, since life expectancy means that half the population lives to that age and the other half lives

longer, from a statistical standpoint this means that every other plan participant is planning to live in poverty. Where tax incentives support DB plans, it doesn't seem inappropriate to require some or all of a benefit obligation to be based on a guaranteed lifetime annuity.

One of the great strengths of the Academy is the tireless commitment of two unique and dedicated groups of individuals. First are the volunteers who contribute endless hours of time beyond their paid employment. The Pension Practice Council and its committees have grown from 70 to 137 members over the past two years—a vivid indication of the dimension of the challenges we face and our willingness to commit to solving them. Easing that effort are skilled Academy staff members, who are always willing to go the

Where tax incentives support DB plans, it doesn't seem inappropriate to require some or all of a benefit obligation to be based on a guaranteed lifetime annuity.

extra mile. For making my job quite a bit easier, special thanks to Joanne Anderson, Lauren Bloom, Noel Card, Ron Gebhardtshauer, Heather Jerbi, Rick Lawson, Linda Mallon, Mark Paster, Anne Richardson, and Steve Sullivan. I owe a debt of gratitude to all of you and many others. Thanks!

Ken Kent will take the reins as vice president for pension issues in November, and I know he will do an outstanding job. I pass along to him the continuation of many existing paths, as well as the discovery of exciting new ones. Happy trails. ▲

JOHN PARKS, president of MMC&P Retirement Benefit Services, Inc. in Pittsburgh, is the editor of the *EAR*. He completes his term as the Academy's vice president for pension issues in October.

ANALYSIS OF THE PROPOSALS

The Academy believes that the law should encourage individuals to save for their retirement and agrees that appropriate simplification of the rules for making contributions to savings and retirement accounts would certainly encourage savings contributions. While several aspects of the administration's proposal have merit, including the simplification of the definitions of highly compensated employees and compensation, simplification of nondiscrimination tests that would make it easier for some plans to pass, exemption of plans from the average deferral test if the amount deferred by the non-highly compensated employee is a large percentage of pay, and a change to the rate of matching contribution that will satisfy the safe harbor, there are advantages and disadvantages to each. We have outlined several aspects of the proposals that concern us.

REDUCTION IN FUTURE GOVERNMENT REVENUE

The proposals would make important changes in the federal tax system, and it is likely that these changes will have significant revenue and equity effects. In particular, the savings proposal may increase current tax revenues at the expense of future revenues. For example, increased tax revenues could result in a reduction of current deficits, an increase in federal spending, or a reduction in taxes; however, any of these could result in an increase in future deficits. This could have a profoundly harmful effect, particularly in view of the anticipated financial effect of the retirement of the baby boomers and later, longer-living generations on Social Security, Medicare, Medicaid, and Supplemental Security Income.

We believe the micro- and macro-economic effects must be carefully analyzed and studied before changes are implemented. In particular, Congress should balance future expenditures with future revenue before proceeding with the types of changes that would reduce future revenue.

DECREASE IN PERSONAL SAVINGS

It is quite likely that the LSA and RSA proposals will not increase personal savings by low- and moderate-income persons. In fact, they could decrease their savings, as discussed in this and following sections. Since very few of these individuals now contribute the maximum amount permitted, increasing the maximum will have no effect. On the other hand, high-income individuals who are now affected by the income limits that apply to traditional and Roth IRAs and/or the limits on contributions to 401(k), 403(b), and 457(b) plans may increase their savings or, at the very least, transfer savings from other vehicles.

Our experience with employer-sponsored plans strongly suggests that it takes immediate tax deductions to encourage low- and moderate-income workers to save for retirement, as well as employee education and matching contributions. Since

LSAs would have no withdrawal restrictions, individuals with low and moderate incomes would choose LSAs over RSAs and ERSAs, and the proposals might actually decrease retirement savings by these individuals. And since there would be easy access to the LSAs, many of them would likely be tempted to withdraw funds for immediate personal consumption instead of holding them for retirement.

DRAMATIC REDUCTION IN RETIREMENT PLANS

It is quite likely that the proposals could severely undercut the incentive for employers to sponsor retirement plans because owners and other decision-makers could save for their retirement without establishing and maintaining a retirement plan for other employees. This would be especially true in the case of small businesses. The owner would be able to contribute \$15,000 on an individual basis between an LSA and an RSA. If the owner's spouse is included, the contribution could be either \$22,500 or \$30,000. Many entrepreneurs would be content with this level of savings and the estate planning opportunities available to these accounts, and would not, therefore, establish an ERSA or other type of retirement plan for the employees of the business, because the cost of contributing for employees and the administrative burden would outweigh the benefits to the owner.

SIMPLIFICATION OF RULES

As stated above, the ERSA proposal would simplify the tax qualification rules for DC plans, which may encourage some employers to adopt retirement plans for their employees. Simplifying the rules will not, however, necessarily result in a substantial increase in the number of employees covered by retirement plans. If it would, SEP and SIMPLE plans, which are available under current law, would be more popular. While we agree that simplification is an important goal, complexity often results from a desire to be fair and takes into account different fact situations and may, therefore, be preferable in some situations. The cost of complying with complex rules is only borne by those plan sponsors who choose to work with the complexity after determining that the benefits outweigh the costs. The positive effect of simplification on plan sponsorship should, therefore, not be exaggerated.

We believe that the anticipated advantages of simplification may be illusory. Many of the existing discrimination and coverage tests and requirements, other than the top-heavy requirements, would continue to exist. Under the new average deferral test, while highly compensated employees would face no restrictions if the average deferral percentage for non-highly compensated employees is greater than 6 percent (providing the potential for a solid retirement benefit for both groups), the same test would offer little incentive for employers to provide matching contributions for rank-and-file employees above 3 percent. At this rate, the highly compensated employee's aver-

age deferral percentage would be 6 percent, which would represent the maximum an employee could save under the ERSA.

The new nondiscrimination test could be avoided, however, under the two safe harbors outlined in the proposal. As noted earlier, the first safe harbor would be the same as current law, but the second would provide a substantially less generous match (50 percent up to 6 percent of pay) than current law (100 percent up to 3 percent of pay plus 50 percent up to an additional 2 percent of pay). Although the new nondiscrimination test and safe harbors could represent a simplification of existing rules, they may not be as advantageous as initially intended.

The anticipated benefits of eliminating the average benefit test, which is elective, may be overstated. The test is essential for many employers with different plans for different lines of business or different groups of employees. This is particularly true when some of the plans are defined benefit (DB) and some are defined contribution (DC), making aggregation difficult. Such situations are not unusual among larger companies with multiple locations. If the average benefit test were eliminated, it would be important, at a minimum, to accommodate these situations and to liberalize the existing separate line of business rules.

For similar reasons, the anticipated benefits of eliminating permitted disparity and cross testing may also be overstated. These tests are elective provisions, and are only required if an employer decides to push the limits of the rules and is willing to accept the extra complexity the tests involve. Permitted disparity allows a plan sponsor to reflect, to a limited degree, the bias built into the funding of Social Security benefits in favor of lower period workers. With respect to cross-testing, recent changes to Treasury regulations have addressed abuses. Cross testing is essential for employers who want to structure benefits differently for different groups of employees, and it is also important for organizations with DB plans and DC plans that are aggregated to satisfy the minimum coverage requirements.

Finally, we believe that it may be inappropriate to eliminate the option of characterizing only the top paid 20 percent of employees as highly compensated employees. This option helps to compensate for the arbitrary nature of the dollar test for highly compensated employee status, which uses the same dollar amount regardless of where in the country an employer is located and in which industry the employer operates.

DECREASE IN DB PLANS

We are concerned that the proposals do not address DB plans. Over the past two decades, coverage under traditional DB plans has declined from 40 percent to 20 percent of the private workforce, while DC plans and 401(k)s have increased from 17 percent to 43 percent. Today, many employers sponsor only DC plans to provide retirement benefits for their employees. We believe a two-pronged retirement strategy is best, with a DB plan

for minimum income security and a DC plan for retirement asset buildup. Currently, the regulatory playing field favors DC plans. This proposal, by increasing the amounts that can be saved for retirement through tax-favored individual savings accounts, DC plans, and elimination of complex rules, will continue the trend that has disadvantaged DB plans to the point where most employers will likely eliminate their DB plans. We believe that any comprehensive retirement reform must focus on both types of plans and not continue the pattern of legislative and regulatory discrimination against DB plans.

ELIMINATION OF TOP-HEAVY RULES

The ramifications of the complete elimination of the top-heavy rules for all DC plans should be reviewed. If the proposal becomes law, the minimum contribution requirement would not be needed; however, the more rapid top-heavy vesting schedule may be appropriate in certain circumstances. While simplifying pension rules may be worthwhile because it encourages some employers to adopt new plans or maintain existing plans, removing provisions that require plans to provide meaningful benefits, such as top-heavy benefits, to lower paid employees may result in reduced benefits for the most economically vulnerable individuals. On the other hand, limiting the benefits that are provided to higher paid employees discourages employers, especially smaller employers, from establishing any plan, even though such plans benefit both the higher and the lower paid. It is important that Congress balance these concerns as it considers simplification proposals.

TREATMENT OF TAX-EXEMPT ENTITIES

The administration's proposals would result in more equitable treatment of taxable and tax-exempt entities. However, the current rules that apply to 403(b) and 457(b) plans reflect the special needs of tax-exempt employers, and therefore it may not be appropriate to eliminate these plans unless these special needs are addressed. For example, many entities that currently do not need to complete annual discrimination testing would be required to perform these tests, resulting in increased administrative costs. In addition, the consolidation of the different plan types into ERSAs would reduce the amount of tax that employees of these entities could defer in employer-sponsored plans.

SIMPLIFICATION OF THE INTERNAL REVENUE CODE

Every change to the Internal Revenue Code imposes certain fixed costs on plan sponsors and administrators in the form of amendments to plan documents, changes in plan procedures, and changes in plan descriptions. For this reason, we believe that there should not be frequent changes to the code, even if the changes simplify it.

We also believe that, if new simplified options are added,

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existing options should not be eliminated without careful study. Employers who have already set up modest plans that meet their employees' needs should not have to go back to the drawing board. We believe that simplification generally should be adopted only when it represents a significant improvement over existing law, and we do not believe this is necessarily the case with these proposals.

SUMMARY

The administration's proposal for two new savings vehicles (LSA and RSA), as well as a consolidated account for 401(k)s, 403(b)s and 457 plans (ERSA), has been received with a mix of criticism and praise.

The fact that the plans would be funded with after-tax con-

tributions and accumulate tax-free, could provide a strong incentive for employees to save. Nevertheless, with respect to the LSA and RSA plans, it is unclear whether low- to moderate-income workers will increase personal savings. Despite the benefits of simplification, there are also disadvantages in the proposed treatment of nondiscrimination testing, safe harbor rules, cross testing, and top-heavy rules with respect to ERSA accounts.

Furthermore, while the proposal has attempted to simplify existing rules for DC plans, rules affecting DB plans have not been addressed. Simplification for DC plans without similar consideration for DB plans only increases the disparity between the two.

The Academy supports the promotion of options for increasing retirement savings, and we believe that the benefits of the proposed savings accounts should be more closely evaluated before any congressional action is taken. ▲

A New Retirement Paradigm

IT WAS A QUESTION with particular resonance for most of the audience at the closing general session of the March EA meeting: What kind of retirement will we be able to afford?

Not your parents' retirement, warned Brian Perlman, a survey researcher with Mathew Greenwald and Associates.

Baby boomers, who will be living longer than previous generations, can expect the supply-and-demand pressures that have followed them throughout their school and working lives to continue in retirement, influencing everything from medical and long-term care costs to financial instruments.

"The bar has been raised," said Perlman. "If we do what our parents did, we'll be eating cat food in retirement."

A complicating factor, session panelists agreed, is the continuing evolution of retirement planning in this country. The number of defined benefit (DB) pension plans being offered by employers continues to drop in relation to the number of defined contribution (DC) plans.

Both employers and employees prefer DC plans, said James Delaplane, an attorney with Davis & Harman and former vice president for retirement policy for the American Benefits Council. Employees like hav-

ing individual control of their accounts, account portability, and the possibility of more meaningful accrual in shorter service periods, Delaplane said. And employers like the fact that employees like them, as well as the predictability of their costs.

But for employees, DC plans are more risky, Delaplane said, citing the uncertainties of whether the employee will be able to save enough to produce a comfortable retirement, whether market conditions will be favorable when the employee chooses to retire, and whether the employee will outlive his or her accumulated assets.

Unfortunately, these risks are not commonly recognized.

"We have a system that has been designed to let people ignore the uncertainty," Perlman said. "We don't educate people. We have a system designed to promote the 401(k)."

"Employees don't understand the value of defined benefit plans, particularly the mitigation of risks," agreed Mark Beilke, director of employee benefits for Milliman USA.

Even though assets in retirement plans are increasing, more people are managing that money themselves, said Perlman. And their expectations on investment returns are overly optimistic.

For instance, most of today's workers

polled by Perlman believe that their own personal assets will support them in retirement. The reality, Perlman said, is more likely to be closer to the experience of today's retirees, who rely primarily on the government.

Similarly, Perlman said, 60 percent of current workers think they are going to continue to work in retirement. Currently, less than a quarter of retirees continue to work in retirement.

The problem is that people make retirement plans for when they are 65, but give little thought to what they will be doing when they are 85, Perlman said. The longer you live, Perlman said, the more susceptible you are to costly and disabling conditions such as osteoporosis and Alzheimer's disease.

In the current policy climate, it is unlikely that the trend away from DB plans will be reversed, said Delaplane. "Some lawmakers think there is nothing to be done to save the DB system," Delaplane said, "only to slow its disappearance."

Despite this assessment, Beilke urged actuaries in the audience to become more involved in the revitalization of DB plans. "Why wait until you've been dealt the hand? Don't assume somebody else is representing your view," Beilke said. ▲