

Retirement for the AGES

Building Enduring Retirement-Income Systems

American Academy of Actuaries
Forward Thinking Task Force

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AMERICAN ACADEMY
of ACTUARIES

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Panelists

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American Academy of Actuaries

The American Academy of Actuaries is a 17,500-member professional association whose mission is to serve the public and the U.S. actuarial profession. The Academy assists public policymakers on all levels by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.



Overview of the AGES

- What is Retirement for the AGES?
 - Follow-on to “Retirement 20/20”
 - American Academy of Actuaries initiative
 - A framework for retirement system design
- What are the AGES principles?
- What else is involved?
 - Scorecards!
 - Forum on April 28



The Spirit of “Retirement 20/20”

- Society of Actuaries initiative launched in 2006
- Design a retirement system from the ground up
 - Questioned whether either DB or DC systems really work
 - Focused on best ideas from around the world
 - *What could be; principles - rather than solutions*
 - *What we need to achieve - not how to achieve it*
- Over 4 years and 3 conferences
 - Identified key drivers of successful retirement systems
 - 2010 conference presented models:
 - Retirement systems that embodied these ideas
 - Demonstrated how principles could work



Retirement for the AGES

- American Academy of Actuaries (Academy) initiative
 - In 2010, the Academy's Pension Practice Council decided to:
 - Create a “Forward-Thinking Task Force”
 - Build on ideas from Retirement 20/20
 - Identify guiding principles for a robust retirement system
 - Introduce these principles into policy discussions
 - Focuses on retirement plan design principles
 - Does not address universal coverage or adequacy
 - Presumes Social Security system remains in place
- “Retirement for the AGES” synthesizes Retirement 20/20 ideas into 4 key categories



AGES: Why Should You Care?

- Retiree income affects U.S. economic performance
- Ability to retire securely also provides:
 - Less reliance on community and family
 - Opportunities for younger workers
- Goal: to facilitate retirement security for all Americans
 - Address shift in roles/risks to employers and employees in voluntary system
 - Retool laws, rules, regulations and practices to support AGES principles

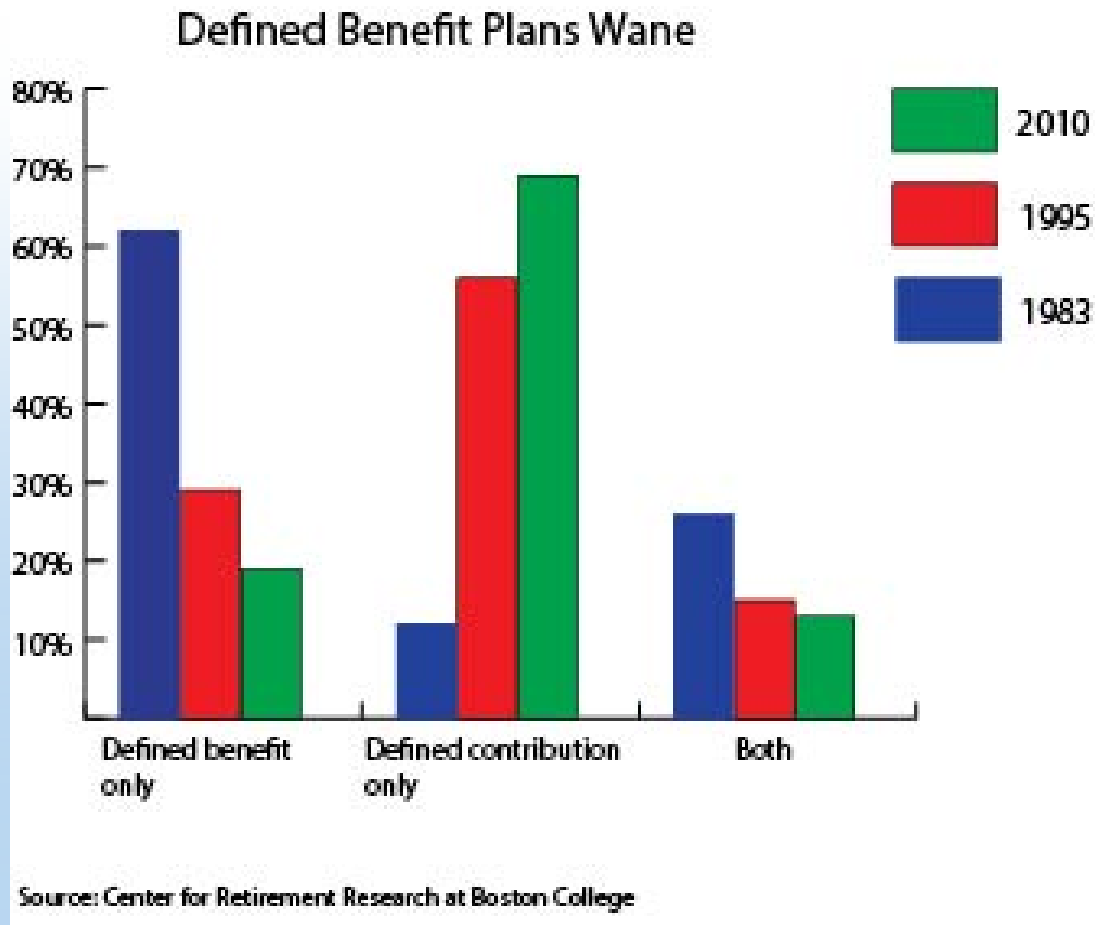


AGES: Why Should You Care?

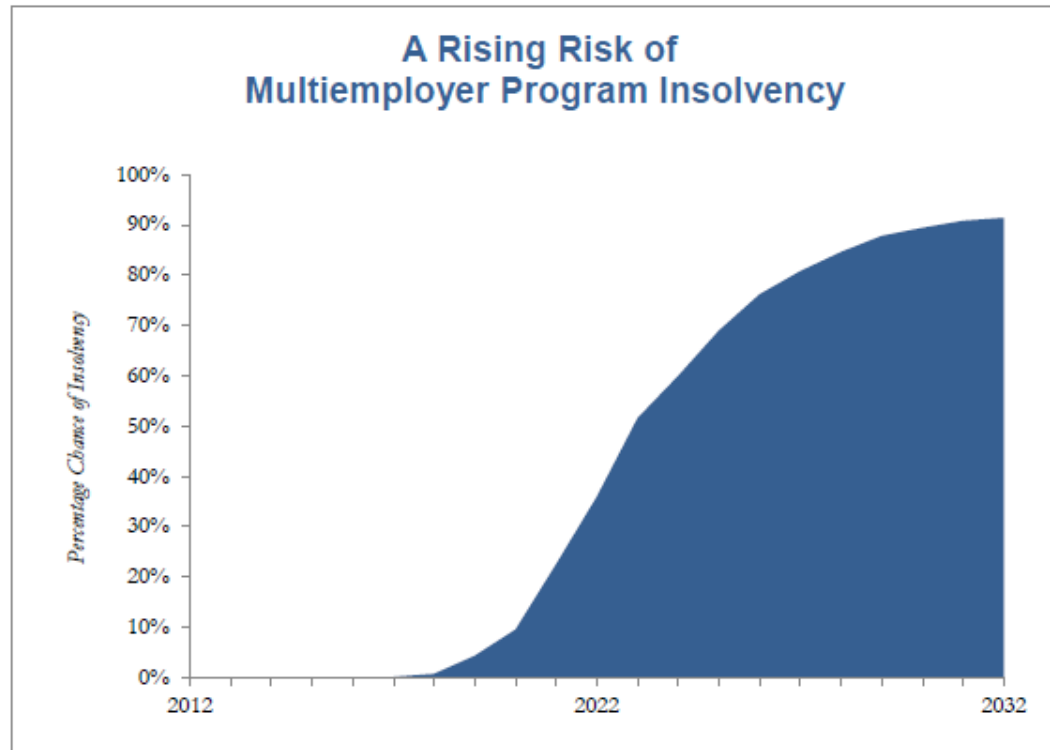
- What is America's "Retirement Income Policy"?
- 4 in 10 retirees rely primarily on Social Security benefits
- Lifetime income coverage (DB) decline
- Public sector pension plan stress
 - Inability or unwillingness to fund
 - Pension reform efforts
- Multiemployer system under stress
 - PBGC insurance fund headed towards insolvency
 - Legislative changes urgently needed



AGES: Why Should You Care?



AGES: Why Should You Care?



Source: FY 2012 PBGC Exposure Report



The AGES Principles

- **A**lignment
 - Are stakeholder roles, choices and skills aligned?
- **G**overnance
 - Does structure support sound decisions and actions?
- **E**fficiency
 - Is retirement income maximized, with controlled risk?
- **S**ustainability
 - How are costs allocated? Are shocks survivable?



Alignment



Alignment

- Key stakeholders
 - Employers
 - Individuals
 - Society (current and future taxpayers)
- Proper alignment of roles and skills
 - Redefine employer role
 - Improve individual decisions
 - Protect society from suboptimal outcomes



Alignment

- Redefine employer role
 - Traditional role – establish, sponsor, administer, and contribute to plans
 - Alternative alignment
 - Use third party to manage and administer plans
 - Improve retirement/financial literacy of employees
 - Collect and transmit employee contributions
 - Advantages
 - Better aligned with core business
 - More transparent
 - Standardized disclosure and fees
 - Not totally dependent on employer



Alignment

- Improve individual decisions
 - Limit unstructured choices
 - Incorporate “auto” features and defaults
 - Employ professionals
 - Provide incentives in tax and other policies



Alignment

- Protect society from suboptimal decisions
 - Develop laws and regulations that enhance financial security systems
 - Balance voluntary incentives and mandatory requirements



Governance



Governance

- Process by which decisions are made and implemented
- Key attributes
 - Stakeholder participation
 - Transparency
 - Accountability
 - Administration in accordance with law
 - Adherence to policies
 - Effective delivery of benefits



Governance

- Key building blocks
 - Clearly define roles and responsibilities
 - Reduce real and potential conflicts of interest
 - Recognize and manage competing needs
 - Staff appropriately



Governance

- Clearly define roles and responsibilities
 - Define purpose and goals
 - Ensure proper funding
 - Monitor operational compliance
 - Establish transparent procedures
 - Ensure execution of roles and responsibilities



Governance

- Reduce real and potential conflicts of interest
 - Require proper disclosure
 - Emphasize fiduciary responsibility
 - Avoid moral hazard



Governance

- Recognize and manage competing needs
 - Anticipate unintended consequences
 - Balance competing interests
 - Establish appropriate legislation, regulations, and rules
 - Ensure strong oversight
 - Incorporate disincentives for excessive risk taking
 - Use self-adjusting mechanisms



Governance

- Staff appropriately
 - Engage independent experts
 - Include representatives of key stakeholders
 - Establish explicit procedures and transparent mechanisms for appointments
 - Disclose remuneration policy and other terms



Efficiency



Efficiency

Efficiency promotes maximizing income at sustainable levels

- Lower plan costs
- Broaden participation
- Minimize leakage
- Pool risk
- Narrow variability



Efficiency

- Lower plan costs
 - Encourage economies of scale
 - Establish regional or national plans that any employer can join
 - Standardize fees
 - Ensure fees are fully transparent



Efficiency

- Broaden participation
 - Provide employees with access to payroll deduction plan
 - Reduce or eliminate age and service requirements
- Minimize leakage
 - Provide incentives for lifetime retirement income
 - Encourage reporting as lifetime income



Efficiency

- Pool risk
 - Encourage multiple distribution methods, by for example:
 - Offering a managed account with a longevity annuity
 - Including immediate annuities
 - Fixed or variable income
 - Allow partial annuitization
 - Limit guarantees to what is needed



Efficiency

- Narrow variability
 - Reduce risk as retirement approaches
 - Dedicate portion of accumulation to retirement income
 - Stress reliability and consistency of income



Sustainability



Sustainability

Sustainable systems must address multiple issues:

- Intergenerational equity
- Proper cost allocation
- Market shocks
- Balancing sustainability and adequacy



Sustainability

- Intergenerational equity
 - Retirement plans are essentially deferred compensation
 - Plans need to be adequately funded to avoid burdening future generations
 - Benefits that are too expensive to fully fund may not be sustainable



Sustainability

- Proper cost allocation
 - Costs should be reasonably allocated among stakeholders
 - Risk involves uncertainty, costs will also be uncertain but must be fairly allocated
 - Tax incentives affect cost to taxpayers and society
 - frequent changes affect cost allocation



Sustainability

- Market shocks
 - Financial crises are inevitable
 - Plans need mechanisms to deal with crises
 - Funding cushions
 - Adjustment of funding costs
 - Adjustment of benefits
 - Risk sharing enhances sustainability



Sustainability

- Balancing sustainability and adequacy
 - Little or no risk in plan enhances sustainability but decreases benefits or adequacy
 - Excessive risk in plan makes crisis inevitable and challenges sustainability
 - Self adjusting systems may enhance both by auto-changing:
 - Allocation or level of cost
 - Retirement ages
 - COLAs or other benefit provisions



Summary

A set of principles to consider when evaluating retirement systems

- Alignment of roles that properly matches the skills of the stakeholders
- Governance that provides a structure that supports sound decisions and actions
- Efficient systems that maximize retirement income while controlling risk
- Sustainable systems that allocate costs equitably among generations and that can survive market shocks



Sample Scorecard

Sample For Illustrative Purposes Only

RETIREMENT FOR THE AGES PROPOSAL/PLAN SCORECARD

PROPOSAL/PLAN	XYZ Act, S. 1001		
Description/ Overall Grade (A-F)			B
Principle	Description	Comments	Grade
Alignment	<ul style="list-style-type: none"> Aligns each stakeholder's role with their skills Redefines employer's role by placing responsibility for important roles with those appropriate entities Helps individuals by structuring their choices to be well-defined and enhance good decision making Develops systemic ways to enhance financial security through appropriate levels of laws and regulations 		A
Governance	<ul style="list-style-type: none"> Clearly defines roles and responsibilities, and acts in accordance with them Reduces real and potential conflicts of interest Recognizes and manages competing needs Staffs boards with financial and other professionals who possess relevant expertise 		B
Efficiency	<ul style="list-style-type: none"> Allows smaller plans to group together, with standard and transparent fees to lower plan costs Provides consistent opportunities to accumulate assets during working lifetime to enhance participation and coverage Minimizes leakage for non-retirement benefits during accumulation and payout phases Encourages pooling and effective risk sharing so funds can provide lifetime income Incentivizes narrowing the variability of benefits by fostering risk hedging and allowing for pricing benefits and guarantees 		C
Sustainability	<ul style="list-style-type: none"> Promotes intergenerational equity Allocates cost properly among stakeholders Withstands market shocks Maintains balance between sustainability and adequacy 		B

For each principle:

(+) Feature meets principles

(-) Feature does not meet principles

(*) Feature where there is not enough information to determine impact



Next Steps

- Scorecard will evaluate existing proposals and plans against AGES principles
- Going forward, Academy will publish new scorecards as new plans/proposals come up.
- April 28 forum in DC
 - Meet with stakeholder representatives of “scored” proposals/plans
 - Discuss current proposals to address shortfalls of current systems
- Website: www.actuary.org/retirement-for-the-ages



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Questions?

