Leave Retirement to the Professionals, Actuaries Say

By Kerry Pechter *Thu, Jan 23, 2014*

A new report from the American Academy of Actuaries posits four basic principles that, if followed, it believes will lead to better pension plans and more secure retirements for participants. Relieving employers of plan sponsorship is one idea.

If the keys to the domestic retirement income industry were handed over to America's actuaries—those brainy, well-compensated civil engineers of the insurance world—what vehicles would they drive and where would they steer them?

Until this week, one could only guess. But a new report from the 17,500-member American Academy of Actuaries, "Retirement for the AGES: Building Enduring Retirement-Income Systems," posits four basic principles that, if followed, it believes will lead to better pension plans and more secure retirements for participants.

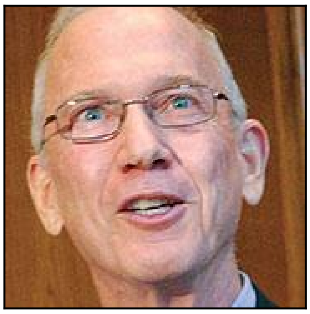
The 23-page document, prepared by the Forward Thinking Task Force of the AAA's Pension Practice Council, describes the four principles as Alignment, Governance, Efficiency and Sustainability. They represent ideals that probably wouldn't surprise anyone in, say, Canada or Denmark. But in the U.S., some might call them radical.

If followed, the document makes clear, those principles would lead to defined contribution and defined benefit plans that, compared to the typical 401(k) plan, would be more outcome-driven, run by disinterested pension professionals, and much more focused on fulfilling the needs of the participants.

For instance, the discussion of the "Alignment" principle suggests that the current situation, where employers sponsor plans and participants manage their own money, is far from optimal. Pensions can be a headache for sponsors, and most rank-and-file participants, who may not even file their own tax returns, have no business managing something as fragile as a nest egg, the report suggest.s.

The report points to TIAA-CREF, the centralized, non-profit retirement plan that allows university faculty and staff to keep the same plan even as they move from one institution to another, as one example of all four principles in action.

"There are characteristics of TIAA-CREF that align well with the principles in the report," said Don Fuerst (left), one of the authors of Retirement for the AGES. "The benefits are portable and there's very little leakage. We'd like to encourage systems like that. Collective management of funds isn't essential. You could have a successful system without it. But that would be a favorable aspect. We'd like to see stronger rules about leakage."



The shift of DC plan savings into adviser-managed IRAs when participant changes jobs—IRA assets now outnumber 401(k) assets—represents a loss of alignment, he said, largely because of the higher costs, greater risk-taking and conflicts of interest that often characterize the retail realm, relative to the institutional.

"The practice of accumulating money into 401ks and then rolling them into IRAs isn't the most effective way to create retirement income. When money is rolled into IRAs, it's often managed by financial advisors, and their interests are not necessarily aligned with the retirement needs of participants."

The white paper's section on Governance seems to be discussing mainly defined benefit pension plans, with references to unions and participant representatives on boards. Indeed, it uses the Ontario Teachers' Pension Plan as an example. But Fuerst said the principles are suitable for all types of pensions.

"The scope is not limited to private or public sector, or defined benefit or defined contribution," he told *RIJ*. "It tries to articulate the key principles that are important in designing any system to deliver retirement income. These are elements that could make any plan more effective."

In the section on Efficiency, the paper addresses the potential to reduce costs and improve outcomes through economies of scale (regional or national plans sponsored by financial institutions) and risk-pooling (the use of longevity insurance or immediate income annuities in tandem with systematic withdrawal plans in retirement.

The fourth principle in the paper is Sustainability. Given the vicissitudes of the economy and the finite life-spans of most companies, many pension plans have historically failed to realize their ambitions. The paper points admiringly to the adoption of "sustainability factors" in national pension plans overseas, where the retirement age and benefit levels have been indexed to changes in fertility or mortality.

As might be expected when the actuaries are the authors, the paper shows an implicit faith in the laws of large numbers and the benefits of risk-pooling. It also seems to take for granted that producing the greatest good for the greatest number is the proper goal of pension stakeholders.

Others might argue that an individual has the best chance for retirement success through personal effort, astute risk-taking, and departure from the herd.

The AAA, which is responsible for the actuarial profession's public policy arm (as opposed to the Society of

Actuaries, which is the professional development arm) hopes that “Retirement for the AGES” will have an impact in Washington during the coming year.

“We’ve already had a briefing at the Capitol for congressional staff members,” Fuerst said. “There were people there from a number of different committees. We sent a copy of the report to [deputy assistant Secretary of the Treasury] Mark Iwry and other people on the Hill. We’re going to hold a forum in Washington in April, and host a further discussion of theses issues. We hope this gets a lot of attention.”