

# **The Pension Challenge**



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## Risk Transfers and Retirement Income Security

EDITED BY

Oliva S. Mitchell and Kent Smetters

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## **Preface**

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In the United States, as in other developed nations, the workforce of the future promises to be quite different from that which we have known in the past. The age distribution has morphed from a pyramid shape, with numerous children on the bottom and few elderly at the top, to a rectangle shape, with about the same number in each age bracket up to age 65. Meanwhile companies have been remaking the workplace over this same period, requiring ever-more skilled labor, more flexible and integrated work teams, and redefining what it means to be an employee working at a company, as global markets integrate.

In this book we explore how these workforce and workplace changes are altering the form and design of employee benefits, and what the future portends. Recent major benefit developments include the 401(k), managed care in the medical field, and the opportunity for even less-skilled workers to access company stock participation. The greater workplace diversity has been complemented by nontraditional benefits including child and elder care, flexible medical benefits, employee assistance programs, and investment education. We evaluate these trends and go beyond, by assessing legal and benefits definitions of the word “employee,” along with new ways to design benefit plans. Perspectives from academics, employers, consultants, lawyers, and labor educators offer guideposts for benefits of the future.

Sponsorship for the work leading to this volume was generously provided by the Wharton School, as well as two important University of Pennsylvania institutions, the Boettner Financial Gerontology Center and the Penn Aging Research Center. We are also grateful for support from the Pension and Welfare Benefits Administration of the US Department of Labor. The Pension Research Council benefits from the invaluable efforts of our Senior Partners and Institutional Members, and the careful attention of Victoria H. Jo and Joseph V. Hirniak. On behalf of the Pension Research Council at the Wharton School, we thank each of these collaborators, along with the editors and contributors who brought this work to fruition.

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**The Pension Research Council**

The Pension Research Council of the Wharton School at the University of Pennsylvania is an organization committed to generating debate on key policy issues affecting pensions and other employee benefits. The Council sponsors interdisciplinary research on the entire range of private and social retirement security and related benefit plans in the United States and around the world. It seeks to broaden understanding of these complex arrangements through basic research into their economic, social, legal, actuarial, and financial foundations. Members of the Advisory Board of the Council, appointed by the Dean of the Wharton School, are leaders in the employee benefits field, and they recognize the essential role of social security and other public sector income maintenance programs while sharing a desire to strengthen private sector approaches to economic security.

More information about the Pension Research Council is available at the web site: <<http://prc.wharton.upenn.edu/prc/prc.html>>

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## Notes on Contributors

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**Zvi Bodie** is Professor of Finance at Boston University School of Management; he also serves on the Pension Research Council Advisory Board and is a member of the Financial Accounting Standards Board Task Force on Interest Methods. Previously he visited Harvard's School of Business Administration and served on the finance faculty at MIT's Sloan School of Management. His research interests include investment, portfolio choice, and finance. Dr Bodie received the Ph.D. in economics from the Massachusetts Institute of Technology.

**David Cummins** is Harry J. Loman, Professor of Insurance and Risk Management at the Wharton School of the University of Pennsylvania. He is the Executive Director of the S.S. Huebner Foundation. He received his Ph.D. from the University of Pennsylvania.

**Suzanne Doyle** is a Ph.D. student at the School of Economics, University of New South Wales in Sydney, Australia.

**Arthur Fliegelman** is Vice-President and Senior Credit Officer in the Financial Institutions Group of Moody's Investors Service where he serves as lead analyst for a portfolio of life insurance companies and evaluates insurance company creditworthiness. Previous positions include principal at A. Fliegelman & Associates, an investment research and consulting firm specializing in the insurance industry; analyst at Salomon Brothers specializing in insurance company investment issues; senior analyst in CIGNA Corporation's investment affiliate responsible for coordinating the company's insurance and investment process; and investment consultant with Hay Associates. Mr Fliegelman received his MBA in finance and insurance from the Wharton School. He is also a Chartered Financial Analyst and an active member of the New York Society of Security Analysts; he is also Vice-Chair of the NYSSA's Committee for Improved Corporate Reporting.

**Peter Forsyth** is a Professor of Computer Science at the University of Waterloo. His research interests concern numerical solution of partial differential equations, solution techniques for large sparse matrices, and computational finance. Previous positions include Director of the Institute for Computer Research at Waterloo, President of Dynamic Reservoir Systems, and a Senior Simulation Scientist with the Computer Modelling Group.

## **xvi Notes on Contributors**

**Jeremy Gold** is Proprietor of Jeremy Gold Pensions in New York. He received his Ph.D. in Insurance and Risk Management from the Wharton School of the University of Pennsylvania.

**Marie-Eve Lachance** is a Ph.D. student at the Insurance and Risk Management Department of the Wharton School.

**Christopher M. Lewis** is Managing Director of the Enterprise Risk Advisory and Technology firm NetRisk and an Instructor-in-Residence in the Finance Department at the University of Connecticut. His areas of expertise include the management and measurement of natural disaster risk, operational risk, and the contingent pension liability of the Pension Benefit Guaranty Corporation. Previously Mr Lewis assisted agencies of the Federal Government (e.g. OMB and OFHEO) and private sector clients in the development and implementation of sound risk management programs.

**Raimond Maurer** is Professor of Investment, Portfolio Management, and Pension Systems Goethe University Frankfurt/M. His research focuses on the insurance and mutual fund industry, investment analysis, real estate finance, and pension systems. He is a Member of the German Society of Insurance Mathematics, the German A.F.I.R. Group (Actuarial Approach for Financial Risk), and Research Fellow of the Center for Financial Studies. He received his Doctorate and Habilitation in Business Administration from Mannheim University.

**Moshe Arye Milevsky** is Associate of Professor of Finance at the Schulich School of Business, York University, and the Executive Director of the Individual Finance and Insurance Decisions Center at the Fields Institute, Toronto, Canada. His areas of interest span finance and insurance, with recent research examining mortality-contingent claims. He received his Ph.D. in Finance from York University.

**Olivia S. Mitchell** is the International Foundation of Employee Benefit Plans Professor of Insurance and Risk Management, and Executive Director of the Pension Research Council, both at the Wharton School of the University of Pennsylvania, and also a Research Associate at the National Bureau of Economic Research. Her research focuses on private and public insurance, risk management, public finance and labor markets, and compensation and pensions, with a US and an international focus. Previously she taught at Cornell University, visited Harvard University and the University of New South Wales, served on the US Department of Labor's ERISA Advisory Council, and served on the Board member for Alexander and Alexander Services, Inc. She recently served on President Bush's Commission to Strengthen Social Security. She received Ph.D. in Economics from the University of Wisconsin-Madison.



## Notes on Contributors xvii

**Robert Palacios** is Senior Pension Economist in the Social Protection Unit of the World Bank. He was a member of the team that produced the Bank's major policy paper on global pension system reform, and since then he has worked in Africa, Asia, Eastern Europe, and Latin America. He is also responsible for managing the World Bank's "Pension Reform Primer" an applied research working paper series. His current interests include estimating unfunded pension liabilities, managing public pension reserves, and converting defined contribution balances into annuities.

**John Piggott** is Professor of Economics at the University of New South Wales in Sydney, Australia. His research interests include pension investments and the determinants of lifetime accumulation and decumulation. He received the Ph.D. in Economics from the University of London.

**David Rajnes** is a Research Associate with the Employee Benefit Research Institute (EBRI) in Washington, DC. His work focuses on issues related to retirement and labor markets including the Retirement Confidence Survey. Previously he served as a statistician at the US Bureau of the Census, and he has also served as a consultant on pension reform and related issues for the US Agency for International Development, the World Bank, the International Labour Office, and the International Monetary Fund. He has graduate degrees in economics from both the American University and Johns Hopkins University.

**Krishna Ramaswamy** is Edward Hopkinson, Jr Professor of Investment Banking and Professor of Finance at the Wharton School of the University of Pennsylvania. Dr Ramaswamy received the Ph.D. from Stanford University.

**Scott A. Robinson** is an Analyst in the Life Insurance Group at Moody's Investors Service where he tracks national insurers including property-and-casualty, and life and health insurers. Previously he was an AVP for the Trust Company of the West and worked with AXA Financial. He received the Masters Degree in Actuarial Science from Georgia State University, and he is a Fellow of the Society of Actuaries and a member of the American Academy of Actuaries.

**Christian Schlag** is Professor of Derivatives and Financial Engineering at the Goethe University Frankfurt/M. His primary research focuses on valuation of derivative securities and empirical capital market research.

**Kent Smetters** is an assistant professor in the Insurance and Risk Management Department at The Wharton School at The University of Pennsylvania. Previously he worked at the Congressional Budget Office, visited the Stanford Economics Department, and served as Deputy Assistant Secretary for Economic Policy of the US Treasury. His research interests include intergenerational risk sharing and risk sharing within households. He received the Ph.D. in Economics from Harvard University.

## **xviii Notes on Contributors**

**John Turner** is a Senior Policy Advisor in the Public Policy Institute at AARP. Previously he taught at George Washington University; he was a Fulbright Scholar in France; he worked for the International Labor Office; and he also worked at the US Social Security Administration and the US Labor Department. His research interests include global pension reform. He received the Ph.D. in Economics from the University of Chicago.

**Stephen P. Utkus** is a Principal at The Vanguard Group where he leads the R&D group within Vanguard's participant education department. He is responsible for developing education, guidance and advisory programs for participants in employer-sponsored retirement plans. Previously he worked in new product development and investment advisory services at Vanguard; he was also an investment strategist and analyst in a Philadelphia financial planning firm. He earned the MBA in finance from the Wharton School.

**Kenneth Vetzal** is an Associate Professor with the Centre for Advanced Studies in Finance at the University of Waterloo. His research interests focus mainly on numerical valuation of complex derivative instruments. He holds a Ph.D. in Finance from the University of Toronto.

**Jan Walliser** is an economist in the African Department of the International Monetary Fund. His research interests include intergenerational redistribution through fiscal policy, tax reform, macroeconomic aspects of pension reform, and annuitization of retirement income. He received the Ph.D. in Economics from Boston University.

**Heath Windcliff** holds a M. Math degree from the University of Waterloo and he is currently completing his Ph.D. He studies in the Department of Computer Science there. His research interests include the development of mathematical approaches for valuing and hedging exotic derivative securities, and object-oriented techniques in scientific computing.

## Abbreviations

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ABS	Asset-Backed Securities
ACPM	Association of Canadian Pension Management
AIR	Assumed Investment Return
AIME	Average Indexed Monthly Earnings
ALPS	Aircraft Lease Portfolio Securitizations
ARC	Annualized Return on Capital
AS-Funds	Altersvorsorge-Sondervermögen
AWI	Averaging Wage Index
Bakred	German Federal Banking Supervisory Authority
BIC	Banking Investment Contract
bps	Basis Points
CAPM	Capital Asset Pricing Model
CBO	Congressional Budget Office
CBOT	Chicago Board of Trade
CDD	Cooling Degree Days
CDO	Collateralized Debt Obligation
CIM	Commercial Investment Mandate
CLO	Collateralized Loan Obligation
CMBS	Commercial Mortgage-Backed Securities
CME	Chicago Mercantile Exchange
CML	Capital Market Line
CMO	Collateralized Mortgage Obligations
CPP	Canada Pension Plan
CPPIB	Canada Pension Plan Investment Board
CRRA	Constant Relative Risk Aversion
CSSS	Commission to Strengthen Social Security
CTE	Conditional Tail Expectation
DAX	German Stock Index
DB	Defined Benefit
DC	Defined Contribution
DSC	Deferred Sales Charge
EBRI	Employee Benefit Research Institute
EETC	Enhanced Equipment Trust Certificates
EGTRRA	Economic Growth and Tax Relief Reconciliation Act of 2001
EMTR	Emerging Market Trade Receivables
EP	Employee Pension
EPS	Earnings-Per-Share

## **xx Abbreviations**

ERISA	Employee Retirement Income Security Act of 1974
ESOP	Employee Stock Ownership Plans
ETC	Equipment Trust Certificates
ETI	Economically Targeted Investments
EV	Equivalent Variations
FDIC	Federal Deposit Insurance Corporation
FILP	Fiscal Investment and Loan Program
FRN	Floating Rate Note
GAO	General Accounting Office
GDP	Gross Domestic Product
GIC	Guaranteed Investment Contract
GIPF	Government Pension Investment Fund
GMIB	Guaranteed Minimum Income Benefits
HDD	Heating Degree Days
HELOC	Home Equity Lines of Credit
IA	Individual Account
IA	Immediate Annuities
ICI	Investment Company Institute
IFSSR	Investment Fund of Social Security Reserves
IPA	Individual Pension Account
IPB	Irish Pensions Board
IRR	Internal Rate of Return
IRS	Internal Revenue Service
KAGG	German Investment Company Law
LIBOR	London-Interbank-Offer Rate
MAR	Market Value Adjustment
MEL	Mean Excess Loss
MER	Management Expense Ratio
MOHLW	Minister of Health, Labor, and Welfare
NCEO	National Center for Employee Ownership
NEPA	National Energy Policy Act
NP	National Pension
NTMA	National Treasury Management Agency
NZSE	New Zealand Superannuation Fund
OASDI	Old age survivor and Disability Insurance
OECD	Organization for Economic Cooperation and Development
OLS	Online Library Service
OSFI	Office of the Superintendent of Financial Institutions
P&L	Profit and Loss
P-AL-B	Professional, Arms-Length Board
PBGC	Public Benefit Guaranty Corporation
PCS	Property Claims Services
POB	Pension Obligation Bond
PWSPC	Pension Welfare Service Public Corporation

**Abbreviations xxi**

REXP	German Bond Index
RMBS	Residential Mortgage-Backed Securities
S&P	Standard & Poor's
SE	Shortfall Expectation
SERPS	State Earnings Related Pension Scheme
SPDA	Single Premium Deferred Annuities
SPIA	Single Premium Immediate Annuity
SPR	Special Purpose Reinsurer
SPV	Special Purpose Vehicle
STRS	State Teachers Retirement System
TCE	Tail Conditional Expectation
TIAA-CREF	Teachers Insurance and Annuity Association College Retirement Equities Fund
TSP	Thrift Savings Plan
USDOL	US Department of Labor
VaR	Value at Risk
VIA	Variable Immediate Annuities
YMCA	Young Men's Christian Association