

AMERICAN ACADEMY *of* ACTUARIES

Objective. Independent. Effective.

Retirement for the AGES Assessment

Forward Thinking Task Force

Proposal: USA Retirement Funds

Grade: A-

In *The Retirement Crisis and a Plan to Solve It*, a white paper by U.S. Senator Tom Harkin (Iowa), he says: “USA Retirement Funds are innovative, privately run, hybrid pension plans that incorporate many of the benefits of traditional pensions while substantially reducing the burden on employers. Under this proposal, there would be universal access to USA Retirement Funds through the existing payroll withholding systems for those who do not already have access to a retirement plan, and anyone participating would have the opportunity to earn a cost-effective and portable source of retirement income. USA Retirement Funds would have professional asset management and give people an easy way to pool their risk with other active employees and retirees. Importantly, USA Retirement Funds would also allow employers to offer a secure retirement benefit without taking on management responsibility or financial risk.”

While a separate bill proposed by Sen. Harkin would include provisions to strengthen Social Security, this scorecard focuses specifically on the USA Retirement Funds Act, which addresses employer-sponsored retirement plans, often referred to as “Tier 2” plans. This evaluation is focused solely on *Title I – USA Retirement Funds*.

Source Material

- *The Retirement Crisis and a Plan to Solve It*, Chairman Tom Harkin, U.S. Senate Committee on Health, Education, Labor and Pensions, July 2012. Available at: <http://www.harkin.senate.gov/documents/pdf/5011b69191eb4.pdf>.
- *Harkin Unveils Legislation to Address Retirement Crisis, Rebuild Private Pension System*, Jan. 30, 2014. Available at: <http://www.help.senate.gov/newsroom/press/release/?id=841825d1-509e-4934-9d7e-968d0853b795&groups=Chair>.
- Text of *S.1979, USA Retirement Funds Act*. Available at: <http://beta.congress.gov/bill/113th-congress/senate-bill/1979/text>.

USA Retirement Funds

Alignment

B+

Description

- 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.

Application of Principles

+ Employer's required role is limited to auto-enrolling employees and processing employee contributions, but employers could contribute up to \$5,000 per year if done "uniformly" (uniform dollar amount or percentage of pay, as long as it is not intended to benefit solely the highly compensated employees).

+ Employer with ongoing DB plan or 401(k) with auto-enrollment and "lifetime income" option does not have to do anything new.

+ Employers can offer their own retirement plans in addition to USA Retirement Funds.

+ No apparent employee investment choice or discretion, other than choice of a USA Retirement Fund. Assets held by each USA Retirement Fund would be pooled and professionally managed.

+ Requirement that employers with 10 or more employees provide access to a USA Retirement Fund.

+ Auto-enrollment at 6% of pay encourages broad coverage and participation (starts at 3% in 2015 and increases up to 6% over 4 years). The plan has auto re-enrollment every two years.

+ Provides lifetime income based on contributions and returns, and benefits are slowly adjusted for pooled asset performance by the USA Retirement Fund trustees.

- Employee contributions are limited to \$10,000 per year. Employees may not have adequate education to understand what contribution levels are sufficient to achieve their individual objectives nor how investment risk impacts the likelihood of achieving those objectives.

- While more efficient, the lack of availability of accelerated payments in the event of long-term care needs or disability, etc. prior to age 60 could be a detriment to individuals.

- Participants will need to choose among multiple USA Retirement Funds and may not have the skills to do so.

Legend

(+) feature meets principles

(-) feature does not meet principles

(*) feature where there is not enough information to determine impact or actual impact may depend on stakeholder actions

USA Retirement Funds

Efficiency

A-

Description

- 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.

Application of Principles

- + Benefits are paid in annuity form (with survivor benefits).
- + Use of large-scale pooling and professional management promotes economies of scale and efficient use of markets.
- + Competition could potentially keep costs low and favor plans with good investment performance.
- + Funds are generally not available prior to age 60, other than rollovers for de minimis account balances, minimizing leakage. There is some ability to withdraw funds after age 60 in the event of substantial hardship.
- + Accounts are portable between funds once per year.
- + Prescribed interest and mortality assumptions for plans that self-annuitize should result in benefits that are reasonably similar to what an insurer would be able to provide.
- + Employers with 10+ employees must provide access to USA Retirement Funds for employees.
- + Improves pension coverage, participation, and individual savings.
- + No accelerated payments appear to be available in the event of long-term care needs, disability, etc. prior to age 60.
- + Employee participation is not mandatory but auto-enrollment helps to increase participation.
- Market risks to USA Retirement Funds are asymmetric - favorable performance permits benefit increases, but unfavorable performance may require regulatory approval to make sufficient downward adjustments to benefits.
- Individuals set own contribution levels but may not have adequate basis for understanding of what contribution levels are sufficient to achieve their individual objectives, nor how investment risk impacts the likelihood of achieving those objectives.

Legend

(+) feature meets principles

(-) feature does not meet principles

(*) feature where there is not enough information to determine impact or actual impact may depend on stakeholder actions

USA Retirement Funds

Governance

A-

Description

- 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.

Application of Principles

+ USA Retirement Funds to be approved and regulated by Department of Labor.

+ The funds are governed by boards of trustees, each who meet qualification standards established by Secretary of Labor; participants and employer representative who meet the qualification standards would be permitted to serve and thus allow for representation by stakeholders in the system.

+ Beneficiaries can participate in trustee selection process and petition board of trustees on certain issues.

+ Transparency and disclosure requirements regarding board policies, compensation, and performance.

+ Trustees can gradually adjust benefits under specified procedures to reflect severe economic downturns or better-than-expected returns.

+ Independent “Commission of USA Retirement Funds Funding” will be established to be responsible for providing recommendations to the Secretary of Labor regarding distributions and funding of funds; its role includes setting assumptions to be used for mortality tables, interest rates, and adjustments needed for benefits for mortality improvements.

+ Assets held by each USA Retirement Fund would be pooled and professionally managed.

- Potential for moral hazard if board of trustees determines benefit adjustments - employees and retirees have an incentive to maximize benefits, while employers do not need to contribute to cover shortfalls.

Legend

(+) feature meets principles

(-) feature does not meet principles

(*) feature where there is not enough information to determine impact or actual impact may depend on stakeholder actions

USA Retirement Funds

Sustainability

A

Description

- Promotes intergenerational equity.
- Allocates cost properly among stakeholders.
- Withstands market shocks.
- Maintains balance between sustainability and adequacy.

Application of Principles

+ Benefit levels can be adjusted based on market conditions.

+ Employers are not required to make contributions, provide guarantees, nor take risks they cannot afford.

+ Prescribed interest and mortality assumptions for plans that self-annuitize can be expected to result in benefits that are reasonably similar to those an insurer would be able to provide.

+ Gradual adjustments to benefits due to market conditions would insulate participants from market shocks.

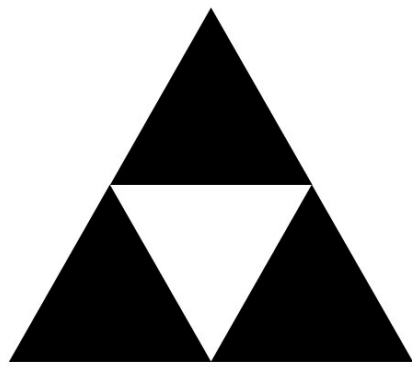
* Whether transfers from one USA Retirement Fund to another are permitted after payout begins, and how the amount of such transfers would be determined, will be decided by each fund.

Legend

(+) feature meets principles

(-) feature does not meet principles

(*) feature where there is not enough information to determine impact or actual impact may depend on stakeholder actions



AMERICAN ACADEMY *of* ACTUARIES

Objective. Independent. Effective.