

# Contingencies

VOLUME 19 / NUMBER 1

Published by the American  
Academy of Actuaries

**PRESIDENT**

Steven Lehmann

**EXECUTIVE DIRECTOR**

Kevin Cronin

**COMMUNICATIONS DIRECTOR**

John Schneidawind

**EDITOR AND ASSISTANT  
DIRECTOR FOR PUBLICATIONS**

Steven Sullivan

**PUBLICATIONS AND MARKETING  
PRODUCTION MANAGER**

Cindy Johns

**ADVERTISING**

Mohanna & Associates

**DEPARTMENT EDITORS**

Thomas L. Bakos

Sam Gutterman

Yan Fridman

Richard T. Zatorski

**PUBLICATION DESIGN  
& PRODUCTION**

BonoTom Studio, Inc.

**EDITORIAL ADVISORY BOARD**

Julia T. Philips, Chair

Dwight K. Bartlett III

Robert L. Brown

Frederick W. Kilbourne

Barbara J. Lautzenheiser

Bruce D. Schobel

Susan E. Witcraft

**INTERNET ADDRESS**

[www.contingencies.org](http://www.contingencies.org)

*Contingencies* (ISSN 1048-9851) is published bimonthly by the American Academy of Actuaries, 1100 Seventeenth Street, NW, Seventh Floor, Washington, DC 20036. For subscription information and customer service, contact the *Contingencies* Subscription Department at the address above or (202) 223-8196. Advertising offices: Mohanna & Associates, Inc., (972) 596-8777, [dawnette@mohanna.com](mailto:dawnette@mohanna.com). Periodicals postage paid at Washington, DC, and at additional mailing offices. BPA circulation audited. (Basic annual subscription rate is included in dues. Nonmember rate is \$24.)

Copyright 2006. All rights reserved. This magazine may not be reproduced in whole or in part without written permission of the publisher. Opinions expressed in signed articles are those of the authors and do not necessarily reflect official policy of the American Academy of Actuaries.

Postmaster: Please send change-of-address notices for *Contingencies*, PO Box 2806, Des Plaines, IL 60019.



## National Treasure

**I**N THIS ISSUE OF *Contingencies*, Dmitry Mindlin suggests that one way to fix America's ailing private pension system is through its accounting procedures. Last summer in *The New Yorker*, best-selling author Malcolm Gladwell proposed an entirely different approach that, as far as I can tell, hasn't shown up on too many other radar screens.

Gladwell starts with something called the "dependency ratio," the ratio of the economically dependent part of a country's population to the part that's actively working. When the national dependency ratio gets too high, too few workers are trying to support too many retirees—the very problem Social Security will be facing in the not-too-distant future.

When the dependency ratio gets too high in a specific company, the same thing happens: too many pensioners, not enough workers to keep the company profitable. Hence, the company goes into bankruptcy and the Pension Benefit Guaranty Corp. gets saddled with the underfunded pension. Everybody loses. Big time.

As a cautionary tale to illustrate this point, Gladwell uses the saga of Bethlehem Steel. At the height of its powers in 1957, when the union-negotiated pension and health care contracts were relatively new, there were 164,000 workers at the company's massive Sparrow's Point plant in Baltimore. By the time it went bankrupt in 2001, 12,000 employees were supporting 90,000 retirees and their spouses. "It had reached," says Gladwell, "what might be a record-setting dependency ratio of 7.5 pensioners for every worker."

The problem, according to Gladwell, was nothing that Bethlehem Steel did wrong; it actually did almost everything right, at least from the standpoint of running a steel company. It responded to increased competition by cutting costs and improving efficiency in the workforce. The problem was the system itself, a system in which individual companies bear the risk and burden of paying all those benefits on their own. And it killed them.

And here's the part of the story that most people probably don't know about: It didn't have to be that way.

After the Second World War, when unions and companies were negotiating this system of pension and health care benefits, the unions believed the best way to make everybody's future secure (workers and companies alike) was to spread the risks. Instead of one company insuring its own employee's health and pensions, companies should pool their resources. That way, if one company or industry fell on hard times — or if demographics changed — it wouldn't necessarily spell its demise.

But the major companies, GM foremost among them, balked at that idea. Too dangerous, they said. Too ... communal? (It was, after all, the era of the two Joes — Stalin and McCarthy.) And so the private pension system took the ruggedly individualistic direction it did.

If anybody understands the value of pooling risk, it's the insurance industry. And I've yet to hear anybody accuse the insurance industry of being communistic. Yet oddly enough, the idea never seems to get much attention as a possible solution to the private pension crisis. The closest the Pension Rights Center's "Conversations on Coverage" seems to get is a proposal for a multiple-employer plan that would encourage more small businesses to offer plans to their employees.

No doubt there are still those who would dismiss the pooling of resources to establish what would amount to a national pension program as absurd and impractical. But aside from its political feasibility, is it an idea worth studying? How does it stack up actuarially? How does it stack up against the rest of the world?

If anybody out there wants to take a crack at answering any of those questions, *Contingencies* has a few pages reserved for you. ●