

**No Substitutions**

I have read with interest the article “Can Education Substitute for Actuarial Exams?” by Rob Brown and Conrad Cicotello in the March/April 2005 issue of *Contingencies*. I do not dispute that the answer they have framed as their conclusion, that education may appropriately substitute at least for the lower numbered technical exams, may be true. Indeed, that has been the experience in a number of other jurisdictions (though I consider the authors’ claim of “virtually everywhere else in the world” to be somewhat exaggerated).

However, I fail to see how that conclusion can be reached from the data they have presented in their article. In fact, one might come to the opposite conclusion. The data demonstrate only that candidates who are students, presumably at university, are proportionally more suc-

cessful than are candidates who are out in the workforce.

There are a number of possible explanations for this phenomenon, many of them far more plausible than the conclusion to which the authors have come. For example, students at university are more in a studying environment with fewer distractions, despite the lure of football weekends and frat parties, and can be much more focused on the needs of the self. Candidates in the work environment are more likely to be faced with the responsibilities of meeting the needs of others: a spouse, a young family, and, of course, an employer. These demands upon the preparatory time of the non-student candidate seem, to me, to be an obvious explanation for the disparity in the data. The data do not tell me that education can substitute for actuarial exams. Rather, the data tell me that non-



students have much different demands upon their time than do students.

It’s unfortunate that the authors have failed to cite at least some of the other available explanations and then followed



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up by demonstrating how those other possible reasons for the resulting data are less plausible than the premise upon which they have built their article.

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### No Actuary Left Behind

The article by Rob Brown in the March/April issue of *Contingencies* advocates abolishing the exam system for Courses 1-4 and suggests that instead, students should be required to take appropriate classes in college. I wholeheartedly disagree with this suggestion.

I'm a big proponent of standardized tests such as SAT, GRE, TOEFL, etc. The reason we have them is that they put everyone on the same level playing field. No matter what high school you went to, you have to take the SAT. Despite the relative differences in student evaluation, students are ultimately compared with the rest of the nation through SAT testing. Under Prof. Brown's logic, we should allow those students who simply took a Kaplan class not to have to take the SATs, and instead be awarded the highest SAT score. Standardized tests ensure that all students have to achieve the same professional standard.

College programs differ from each other. Strictness of professors and quality of education also differ. Additionally, I know of instances of cheating on exams in college, especially in other countries. However, I've never heard a story of a successful cheater on an actuarial exam. In some colleges, finals have the same problems year after year. At other colleges, this would be impossible.

Abolishing the standardized test system is just giving a way to subpar, lazy, and potentially even dishonest students to advance in their careers.

The removal of the exams is usually advocated by college professors whose priority is to attract more students to their classes. However, some professors aren't adequately knowledgeable to talk about all the actuarial topics covered

on an exam. Some are simply not good teachers. I don't trust these professors to maintain the high actuarial standards we have applied to our own profession.

A strong education is a great tool to prepare for an actuarial exam. However, I do not feel that it could ever act as an adequate replacement for the exams. If the Society feels that the exams do not effectively address the educational needs of future members of the Society, they should fix the material, not cancel the exam.

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### Privatization or Ponzi?

I just finished reading Thornton Parker's article, "How Can Stocks Help Social Security?" and a related piece, Steven Sullivan's fascinating "Inside Track," both from the January/February 2005 issue of *Contingencies*. I was so amazed at the tenor of both articles that I felt compelled to write.

Mr. Parker's article examines the thesis that investing one's retirement funds in the stock market is riskier than entrusting them to the political poll-driven whims of the 435 otherwise unemployable individuals who constitute the United States Congress. There is so much for a free-market libertarian (like me) to contest in Mr. Parker's article that I found myself trying to find anything in it with which I could agree.

I found it. Mr. Parker and I can agree that owning an undiversified portfolio composed only of common stocks in an economy that is creating no new wealth is a bad idea. Fortunately, I have found no one engaged in the current debate on Social Security, other than Mr. Parker, who has suggested that solution for private accounts. Thus, he has hypothesized a straw man that he very successfully destroys. Truly, the stock market can't be worse than the Social Security Administration, which has squandered every dime it has ever collected. For those of us with substantially all of our retirement



funds in 401(k) accounts invested in American financial markets, what would Mr. Parker have us do?

Mr. Sullivan's poll of the Academy's staff on their willingness to take unpalatable, financially painful steps to improve the finances of the current Social Security system confirms at least one thing: Americans are coming to grips with the fact that Social Security has never been an insurance program but rather, as the Supreme Court has repeatedly concluded, a welfare program. Once our political leaders admit to that realization, a far better solution for improving its financing would be to eliminate the payroll tax and completely fund the program like all other welfare programs, out of the general treasury (though I've read one lighthearted suggestion that we raise the payroll tax to a combined 20 percent and eliminate the federal income tax).

Even those steps address the wrong problem. The real issue is that Social Security is a bad economic deal and it's worst for those who rely on it most. There are sufficient examples of private-market programs that are structured like Social Security but significantly outperform it economically (the city of Galveston, Texas, is one such example) to prove that privatizing the system is a far better solution than patching it up.

Stripping away the political rhetoric from the current debate in Washington, it appears to me that there are two big issues (and a couple of minor ones) standing in the way of a full privatization of Social Security: uncertainty of investment returns, which creates the so-called safety net concern, and the uncertainty of mortality.

The first issue, simply stated, is that private individuals might invest their retirement account assets so poorly that they don't have a sufficient balance on their retirement date to fund a pension at some minimum level, such as the current Social Security benefit level. That's hard to believe, but it's possible.

The second issue is that people may outlive their pension assets and find themselves destitute. This is, of course, a risk with any finite pool of funds.

It's interesting that both of these issues appear to fit the definition of insurable risks. Assuming that investment options are fairly tightly controlled, it should be a relatively straightforward calculation to assess the chance that a pool of funds collected over a working career might not fund a life pension at some minimal level. From that, it should be relatively straightforward to produce an insurance product that would cover the "safety net" exposure.

Similarly, for a reasonable set of payout parameters (such as a level payout that amortizes the pension fund over the life expectancy of the retired worker), it should be straightforward to produce an insurance product that would cover the risk that people outlive their pension funds.

Finally, with more than 140 million workers contributing to private accounts, the pool of insured risks for these products is huge.

Rather than conducting polls about patching up the current Ponzi scheme (which should have, in any case, been placed in the context of the even more Draconian steps that will be needed to "fix" Medicare, Medicaid, and the national

debt), it seems to me that the Academy could provide more meaningful input into the Social Security debate by enlisting the talents of its members to provide actuarial solutions to the issues that stand in the way of privatizing the program. This would help to provide a better alternative to fixing the finances of the current Social Security system and a better retirement plan to millions of American workers. The fact that such solutions could provide a major new market for the commercial insurance industry is simply an added bonus.

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*Editor's note: Normally, I just shut up and take my medicine. But I did take great pains (I thought) to point out that the poll I conducted among the Academy staff was informal, unscientific, and certainly not an Academy work product. On the contrary, Mr. McConnell should be reassured to know that the Academy is actively engaged in doing just what he suggests, "enlisting the talents of its members to provide actuarial solutions to the issues," regardless of which side of the issue those solutions might favor.*

### Trust Fund

I thoroughly enjoyed the debate between Haeworth Robertson and Dwight Bartlett in the most recent *Contingencies* (May/June 2005). It's always interesting to have two such experts debating the pros and cons of public policy.

However, I do take exception to one statement from Mr. Robertson. He indicates that the ultimate cost of the Social Security program should be no higher if the benefits remain the same. However, the president's individual account program within Social Security adds a new and disturbing benefit, namely the right of inheritance.

Under his program, a deceased participant could pass on his account to his heirs. As a result, money that could once be used to subsidize benefits for the survivors now is subject to withdrawal from the program. What was once an in-

surance program to promote retirement income security thus becomes an estate accumulation vehicle.

This corresponds with the recent efforts by the Republican majority to do the same thing with ERISA. By enlarging limits and eliminating certain excise taxes at death, all the tax benefits associated with the efforts to create retirement income security are now bestowed on estate accumulation.

While I do not mean to impugn the practice of estate building, I believe the extent to which it's built into public policy should be a debate separate from the effort to provide financial security for retirement purposes. Thus, the president's program furthers the transformation of retirement income security into wealth and estate building without having a true and open debate on the role of government subsidies for asset accumulation.

Maybe the Congress should attach a rider to whatever legislative vehicle is put to a vote to change Social Security to eliminate the estate tax altogether!

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*Mr. Robertson responds:* I'm pleased the social insurance articles in the May/June *Contingencies* generated so much discussion, much of which was sent directly to me. Mr. Barney writes that he "takes exception" to my statement, "If benefits under a revised system are no larger than benefits under the present system, the revised system cannot possibly cost more."

His apparent reasoning is that the president's proposed individual account program adds an inheritance benefit with an obvious added cost. However, my statement—as well as my entire article—had absolutely nothing to do with the president's proposal or any other specific proposal. My statement remains true: If benefits are not increased, the cost does not increase—an important principle in view of frequent allegations that a revised system will add "transition costs." ●