Collective Bargaining for Pensions

Proceedings of a conference on

"War Time and Long Range Issues in Collective Bargaining for Pensions"

held at Robert Allerton Park, Monticello, Illinois

February 16-18, 1951

Institute of Labor and Industrial Relations
College of Commerce and Business Administration
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Preface

Approximately 25 specialists in industrial pensions--from Universities, government, labor, management, and consulting firms--met at Robert Allerton Park, University of Illinois, from February 16 to 18, 1951, to participate in a conference on "War-Time and Long-Range Issues in Collective Bargaining for Pensions." They had been invited to discuss informally the problems and prospects of the current trend toward employer-union collective bargaining on pensions. The conference was conducted by the College of Commerce and Business Administration, and the Institute of Labor and Industrial Relations through the Division of University Extension.

The conference was planned to provide an opportunity for an exchange of views and experience among persons from different organizational and professional backgrounds who are involved in negotiating and planning pension programs. However, the participants were not expected to represent the official views and policies of their respective organizations or agencies. It was hoped that they would participate in defining and analyzing the major controversial issues in the field with special reference to problems raised by our current defense-oriented economy. The proponents of different approaches to the pension problem were to be encouraged to explain the considerations lying behind their points of view. This was aimed at finding what basis there may be for reconciliation of the divergent approaches and for exploring degrees of concensus which might be achieved on certain points.

A proposed agenda was circulated among the participants prior to the conference and the final program reflected several changes which were suggested. The chairmen of the sessions were asked to guide the discussion along the general lines of the agenda, but also to give considerable latitude to the participants in determining where they wished to place the emphasis.

The following proceedings were compiled from long-hand notes taken during the sessions. Although statements have been paraphrased and discussions summarized, the form of the proceedings has been designed to preserve the flavor of the interchange of individual opinions and observations. Generally speaking, the personal identity of the speakers has not been revealed although an identifying title is usually employed to indicate whether the speaker was from management, labor, government, university or consulting firm. The participants had an opportunity to review the proceedings to make sure they generally reflected the character of the discussions.

The document attempts to present the ideas, suggestions and points of view which emerged out of the discussion. Since the conference made no effort to reach any general concensus on most issues, these proceedings should not be read in the expectation of finding considered "solutions" to problems or any general "conclusions."

Little or no effort has been made, moreover, to provide a further explanation of terms used or points made than was presented in the discussion itself. In their present form, therefore, these proceedings are not offered to the general reader as a clear well-rounded presentation of the subject of pensions in collective bargaining. They are offered as a summary of a discussion carried on by a group of specialists in the field of pensions, for the information and interest they can provide for other specialists as well as others who have sufficient background to fill in the obvious gaps in information and explanation.

The major work of planning and carrying out the conference was done by Professors John M. Brumm and Phillips L. Garman, with valuable assistance from Professor Charles W. Anrod of Loyola University.

The proceedings were written by Professor Brumm and edited by Donald E. Hoyt, Institute Editor. Notes were taken during the sessions by Louis S. Boffo and Arnold Weber, Graduate Assistants in the Institute.

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Introduction

A welcome from the University of Illinois was extended to the conference participants by Phillips L. Garman of the Institute of Labor and Industrial Relations, and by Earl Strong of the College of Commerce.

The speakers indicated that this conference had three general purposes: first, to permit a free exchange of ideas and experiences from the various persons present with their differing backgrounds and points of view; second, to provide an opportunity for the University representatives to learn something from the others present; and third, if the participants agreed, to produce some sort of publication out of the conference proceedings.

1\. Are Pensions a Significant Answer to the Problems of Old Age in Industry

Chairman: Emmett B. McNatt
University of Illinois

In his introductory remarks, the chairman suggested that the group concentrate at the outset on the broader aspects of pension problems and leave the technical aspects for later consideration. He felt the group was probably agreed on the importance of the old age problem. Current statistics indicate there are now about 11 million aged persons in the United States, and that the figure may reach 17 or 18 million by 1960. This conference was presumably interested in those over 65. Of this group the proportion which is in the work force declined considerably between the late 1800's and 1940. Although there probably has been some shift since 1940 due to the war, the trend at this time is not clear.

Compulsory retirement

The chairman then raised the question: "Should retirement be compulsory?" He noted that Professor Sumner Slichter of Harvard University was opposed to compulsory retirement for the following three main reasons:

1) the loss of national income; 2) the loss of productive manpower from the labor force; and 3) the possibility of manpower problems in case of emergency.

Addressing himself to compulsory retirement, a consultant suggested that its applications to management and to manual labor groups should be considered separately. Provision should be made for management people to retire in an orderly manner from the work force. When members of this group become old it is time for them to get out and make room for the younger trained people -- for "new blood." The situation is different, however, for the factory worker. Whether this man be 16 or 68, all that should matter is his ability to do the job. An arbitrary retirement age is not justifiable. The speaker said that if he were a union man he would insist on infusing new blood into management, but would not want to force out the working man. Unions and managements should get together to establish qualifications and tests of performance or some other methods for determining when a man should retire. An employer stated he did not appreciate the reason for distinguishing between managerial employees and manual workers except, perhaps, in the case of the extreme top management and the least skilled level of workers.

Agreeing with the earlier speaker, a college professor felt that manual workers should be kept at work. He contrasted their situation to that of the college professor, who can find interest in many things and continue his life in a manner relatively undisturbed by his retirement. When a manual worker retires from a job which has been the major activity of his life, he cannot easily find new employment or activity which has any vital significance for him. A consultant agreed with the "theoretical implications" of the position just stated, but pointed to the practical problem of discovering some way of eliminating inefficient people from the work force.

A union man said he favored a definite compulsory retirement age on the ground that our economy is normally short of jobs in both the management and labor market. When he reaches a certain age, an old worker should leave his job, but he ought to have something on which to retire. He could hardly be expected to want to retire if he couldn't continue to support himself.

The consultant who had opened the discussion replied that his opposition to compulsory retirement for the manual worker did not necessarily apply in all contexts. In a period of depression one might favor a program of retiring men still capable of performing their work. A possible formula is found in the experience of the textile industry where between the ages of 65 and 68 the decision on retirement is joint, while after 68 it is at the employer's sole discretion.

The unionist who had supported the idea of compulsory retirement added that a man should lose his seniority on retiring. Thus, if he had to be brought back into the work force, in some emergency such as war, he would return as a new employee and subsequently be among the first to be discharged when there was no longer a manpower shortage. Other union people expressed disagreement with this point of view.

Someone then suggested that the group might profitably distinguish between the problems arising when there is a shortage of jobs and those arising when there is a shortage of work.

Declaring that the problem cannot be solved by any arbitrary decision, another unionist said workers would retire of their own violation if retirement benefits could be made sufficiently attractive. In the depression the problem was not one of forcing the old to retire, but rather one of reducing the work week. No society could function on the basis of forcing a man to give up a job solely because of his age.

Ethical considerations

print

A government man commented that the discussion up to this point had been in terms of changes in the labor market and of certain emergency situations. He asked whether the others felt an "ethical problem" was involved in depriving any man of the right to earn a livelihood -- quite apart from any economic issue and any internal union political problem. Another participant agreed that no one had the right to retire men who are clearly able and willing to work, but pointed out that he was referring to manual workers and that the considerations involved in finding a practical solution to the problems of management people would be quite different. He added that in his opinion a "practical solution" in the case of manual workers would be a joint decision on employability by union and management.

Another person suggested, on the other hand, that since society sets certain restrictions on the age when a man may enter the labor force it reasonably might also regulate the time when he must get out. Opposition to "carrying this logic too far" was expressed by the person who had first raised the question of ethics. He added that the entire question deserved serious consideration.

Costs and adequacy

print

A system of compulsory retirement, if adopted, might raise the cost of pensions anywhere from 25 to 40%, a government man stated. An adequate pension -- however "adequacy" might be defined -- could raise the total cost of pensions to 15 or 18% of payroll, and possibly even higher if other related factors are taken into account. Another member of the group agreed that the increase in costs might be "tremendous" if a formal compulsory retirement age was adopted.

The importance of "adequacy" in any discussion of desirable retirement age was emphasized by several union participants. One of them suggested a rough definition for the term might be: "at least somewhat attractive to the individual." A consultant responded that he knew of pension plans where the company offers a man half his current earnings if he will retire, and where many employees still will not leave.

An economics professor said that in his opinion the problem in retirement stems from the failure to consider physical and psychological factors in retirement. Most thinking on the subject has been in terms only of the economics of the situation, whereas there is a great need to prepare the work force for the physical and psychological aspects of retirement. An education program, started at an early age, might help effect a change in worker thinking. Whereas workers previously thought in terms of a schooling period and a work period, they might now learn to expect a period of preparing themselves for work, a period of work, and finally a period of retirement. In support of this proposal, an employer described the problems his firm has in retiring a man after 65. It is difficult to prove that a man cannot do his job after he reaches retirement age. Much is left to a doctor's decision, he said.

Other participants enumerated additional psychological and sociological factors tending to keep older workers attached to their jobs. A worker's need to feel "important" and "useful" was cited. Allusion was made to the automobile industry where only 5% are said to retire at the permissable retirement age, and to the mining industry where the average retirement age is reported to be close to 65 despite the voluntary retirement age of 60.

A major problem, a government man said, lies in the fact that in the upper age bracket there has been an increase in the number of people capable of doing very good work for a limited period of time although not for any extended period, such as the normal forty hour week. From an individual's point of view, compulsory retirement seems to be a rather simple problem, but when it is viewed from a national perspective and in terms of the 11 to 16 million people in old age categories who are not able to work a full 40 hours a week it becomes a very serious problem -- a problem involving all the manpower of a whole community.

An employer suggested it might be possible for a union and management ~~to agree on a wage~~ scale and a rate of production to be applied to older men who cannot keep up with the standard. In his opinion, however, this would be difficult to carry out. While other members of the group pointed out that this had been done in some cases, there appeared to be agreement it would be very difficult as a general practice.

A consultant felt that the main objection people had to retiring was the fact that they "liked to eat," and that pensions are not enough for people to live on. However, men who have had productive well-paying jobs do ~~not like to degrade themselves by taking less important jobs as~~ they become older, and would prefer to retire if they had an adequate pension. He also called attention to the cost of the so-called "hidden pension" which a company incurs when it keeps on the payroll aged workers who are not sufficiently productive.

A government man pointed to the apparent increase in the number of newspaper advertisements offering employment to men who have retired, and proposed that some way be devised to bring them to older workers' attention. The advertisements suggest the older worker may find an unexpected market for his services which to some extent should help to shift him from his current job to some other more suitable employment.

One participant pointed out that the group seemed to be agreed in principle that an answer to the retirement problem must be found in general terms of a man's employability as he reaches old age.

On this point, a consultant noted that at a recent conference in Washington he had observed that all the participants, representing many different disciplines, had also shifted their emphasis in the discussion from the problem of retirement to the problem of employability.

In his opinion, however, several other factors needed consideration. Productivity of the superannuated is an important factor. Also significant is the effect that an expanding number of older workers will have on national income and on the rate of increase in productivity. The effect might be either to slow down productivity, to stabilize it at a certain level, or to cause it actually to decrease. The business cycle and its relation to total employment and to employment of the aged was an additional important factor. He also suggested there were possibly some anti-cyclical factors involved, such as stabilization of income and consumption of the aged population under an expanded pension program, which might in turn stabilize investment.

"Age 65"

Mr. Cohen of the Social Security Administration was asked to explain why, historically, age 65 rather than some other age has been accepted as the age for retirement. Mr. Cohen said that to the best of his knowledge, nearly everybody concerned with setting up the social security system in 1934 and 1935 seemed to feel that 65 years was the appropriate retirement age, taking into account the provisions of then existing plans, costs and prevailing attitudes. Thinking at the time of the passage of the Social Security Act was based on a depression psychology, which today, in a sense, has been repudiated, and justifiably so in his opinion. However, even though 65 is not a magical age and appears to have been an arbitrary choice, it has not in fact worked out badly.

Someone asked Mr. Cohen whether the actuarial estimates for the social security program were not in fact based on 67 years of age rather than 65. Mr. Cohen replied that actuarial estimates were based roughly on 67 1/2 years as the average age of retirement over the long range. If all eligible workers retired at the age of 65, the additional cost would be about 1% of payrolls. Administration experience shows the current actual retirement age is about 68 1/2.

One participant stated that he felt it was very important to keep the retirement age under Social Security from being lowered and thus greatly increasing the cost of the Federal program. In answer to a question raised as to where the pressure for lowering the age was coming from, discussion brought out that for differing reasons both old and young worker groups often pressed for such a policy.

Returning to the question of why 65 is the accepted normal retirement age, the chairman suggested that in addition to the depression psychology of the time it was also a common practice for insurance contracts to set the retirement age at 65. Other participants, however, knew of contracts setting the age as low as 60 years, and even lower for persons of means desiring to retire earlier. Someone added that the customer could usually set any retirement age for which he was willing to pay the necessary premiums. A university professor stated he has come to the opinion that 65 is too low an age for normal retirement and that an age between 68 and 70 would probably be more reasonable.

Slichter's proposal for employing older workers

At this point the chairman asked whether anyone desired to comment on Professor Slichter's recent proposal relating to a method of helping older workers retain employment in industry. As reported in the Commercial and Financial Chronicle, Thursday, March 23, 1950, Professor Slichter had suggested the following plan: "I believe that immediate steps should be taken......to help workers between the ages of 65 and 70 continue in employment instead of being forced to retire. The best way to do this is to give employers an incentive not to retire physically fit workers before the age of 70......it might be either a penalty or a reward. I believe that a reward is preferable to a penalty. If the employer were penalized for retiring men below the age of 70, he would be discouraged from hiring older workers -- men of 60 or near 60, whom the employer might be willing to hire under ordinary circumstances. If the employer had doubt thse men would be physically fit to work until they were 70 years of age, he would refuse to hire them.

"The method of rewards however has great possibilities. In order that I may be definite and concrete, let me venture a tentative suggestion. Let us assume for the sake of illustration, that the average pension was $75 a month, or $900 a year. An employer who kept a man until the man was 70 years of age instead of retiring him at the age of 65 would be saving the pension system $4,500 in pensions. The employer might be rewarded for keeping men above 65 by being given a rebate of one-third of the resulting saving to the pension fund. In the example I have given, one-third of the saving would be $1,500. If the employer had kept the man until age 68, the pension fund would be saved $2,700, and the rebate of one-third would have given the employer $900.

"This rebate would give management an incentive to find ways of keeping men beyond the age of 65. Furthermore, instead of being a deterrent to management's hiring older workers the rebate would be an incentive. If an employer hired a man at age 62 and kept him until the age of 70, the employer would be given a rebate for the saving made possible in pension payments to the man. Naturally employers would be interested in hiring older workers who showed promise of being efficient after age 65. Then older workers thrown on the market by firms going out of business and by layoffs would find their employment opportunities greatly improved."

Opposition to the Slichter proposal was expressed by a government man on the ground that adoption of the principle of providing subsidies for employment of people over 65 would open the way to demands to extend employer subsidies for employment of people in other categories -- first the physically handicapped, then the mentally handicapped, then "minority" groups, etc.

A consultant added that the Slichter proposal seemed to be predicated on an incorrect assumption that most men want to continue work. In answer to a query as to how he would account for the fact that in many cases where pensions seemed adequate many workers still remained on the job, the consultant suggested that our culture "made a god out of work," but that if we were to change our thinking in terms of retiring at a certain age and if adequate pensions were available people would probably retire.

Physical disability

A government man said that the public program is admittedly deficient in terms of providing a sufficient amount of money to encourage people to retire, and that the people who do retire are probably those physically and mentally incapable of working. The government program attempts only to provide "basic minimums." Also important is the general problem of physical disability -- not just at the normal retirement age but at any time a worker becomes physically disabled. The problems of setting an appropriate retirement age has been given more attention than it deserves, while inadequate consideration has been given to the role of disability benefits in the Social Security program.

Alternatives to pensions

The chairman asked the participants to turn their attention to alternative approaches (i.e., other than pensions) to the problem of old age in industry. The conference program had suggested the following possibilities: wages and savings; family ties; profit sharing plans.

A university professor said he did not think that savings or similar expedients were solutions to ~~the problems of~~ old age, because of the fluctuations of the real value of the dollar and the rising rate of taxation. He thought pensions offered the only feasible answer to these problems.

An employer replied that, ideally, preparation for retirement in old age should be composed of several well-balanced factors such as stock investments, private pensions, government social security, and savings. He acknowledged, however, that it was not realistic to expect many of these means to be available to the industrial worker today.

The professor added that, due to the decline in the interest rate from 6% to 2% over the last 20 years as well as to economic conditions in general, a worker would have to accumulate substantially greater savings in order to get the same benefits provided by a smaller amount of money 20 years ago.

In the opinion of a government man, a major problem was the high cost of illness or disability in a worker's later years, tending to create an atmosphere of uncertainty and fear. The cost of such "terminal illness" is frequently as much as $1000. This problem could be met only through plans insuring hospital and medical expenses in old age. There appeared to be agreement among the participants that current health insurance plans did not meet this particular problem.

The "three layers" of pensions

A consultant said he felt that while pensions are not the complete answer to the problem of old age, they are a significant answer, and that there are really three types or "layers" of pensions: 1) a social-security pension yielding enough income to provide a subsistence standard of living; 2) a private industrial pension which could provide supplementary benefits: and 3) savings, which could provide the individual worker a "luxury" standard of living. The immediate objective, however, should be to take care of the first and second "layers."

Institutional care

Another participant raised the question of providing benefits in kind, such as adequate food and medical care, to the over-age worker through the community. He noted that there are some private institutions in existence today which provide full care for people over 65 for a flat monthly payment. Someone retorted that this appeared to be the old poor house in a new guise.

A government man commented that in 1935, with the establishment of the Social Security program, the country had tried to get away from the old idea of the poor house, but that now it seemed to be returning to the same idea "from a high class approach." He thought the development of nursing homes new kinds of problems -- particularly psychological problems. Special housing developments for old people might help solve these problems. Someone noted that such developments do exist in Florida.

This started a brief discussion over the question with whom old people prefer to live and associate. The group appeared to be uncertain as to whether it was with the old or the young.

The discussion switched to a consideration of the potential political power of organized groups of old people. Statistics were presented indicating that the "aged" constituted 9% of the voters in 1930 and by 1980 would make up 24% of the voting population. It was suggested that old people might turn to politics to occupy their idle time and someone remarked that eight million old people can exercise more "political power" than 45 million young people, because many of the latter are unable to vote or not sufficiently interested in voting. An economist was quoted as having foreseen a future "class war" between the old and the young, rather than between capital and labor. In answer to one participant's remark that, to his knowledge, organizations of old people developed only in Colorado and California and as a result of the depression, another replied that the depression could not fully explain phenomena such as the Townsend movement, which made old people "feel socially and psychologically significant."

Someone noted that the original Social Security Act provided governmental "assistance" to the aged in institutions only if the institutions were private, but that the law has now been changed to grant government assistance even to people in public-supported homes for the aged. States must first meet certain general standards before individuals entering their institutions are given Federal assistance. The speaker felt this amendment to the Social Security Act would result in an increasing number of public and private institutions for the aged.

On-the-job alternatives

Down-grading of old people in a given productive unit, or transferring of them to other more suitable jobs in the community or given labor market, was proposed as another "solution." A plan in Schenectady was mentioned where older workers did not have to meet normal quantitative standards but were paid according to what they produced.

Discussion turned to the alleged difficulties encountered by workers over 40 in finding new jobs. A professor suggested the solution of this problem required the joint efforts of union, management and the community. A consultant observed that many employers hesitate to hire older men on the ground that they will not give enough service to justify the costs of a pension adequate for their needs. Some employers are known to require an employee over 40, if hired, to sign away part of his benefits. A problem of this sort could be met through a more adequate system of governmental social security benefits, said a government man, since a Federal system permits a man to accumulate service credits over his whole life-time of employment regardless of where he worked, providing his types of work were "covered." The consultant countered that in his opinion vesting (to be discussed in later sessions) was the best answer. A union man said he was not inclined to criticize management for not hiring people over 40, since national survival was dependent on maintenance of high productivity to keep ahead of Russian industrial expansion, and, therefore, the best solution was to retire men with adequate pensions. The consultant objected that he saw no reason why employers should not hire men over 40 since they have wider experience that might make them exceptionally valuable to an employer. The important consideration was the individual's physical ability in relation to the demands of the job.

Warning against the dangers of generalization, a professor said that although some men of 40 are better workers than younger men because of wider experience, many over 40 are at a disadvantage in comparison to more youthful workers, and that distinctions need to be made among occupations and individuals. A government man noted that a high percentage of the aged appeared to be engaged in the real estate business, and that this suggested studies might be made of the ways in which certain industries in a given community could profitably use old people. However, since there are many "single-industry towns" where it might not be possible to shift the older worker to a position for which he is better suited at the time, each community needs to plan ahead to provide for sufficient diversity of industry to make possible wider opportunities for aged workers. On this point an employer commented that such a recommendation assumed an unusual flexibility in the industrial set-up within a given community. Factors making for such flexibility, however, are subject to industry-wide patterns which might counteract efforts of local groups to deal with the problem of diversification.

The chairman said that the group appeared to feel there was no single solution to the problems of the aged. He thought it would be valuable for the group to keep in mind the "three layered cake" analogy of the purpose of different kinds of pensions, and suggested that the participants consider the specific responsibility of industry in solving the problems of old age.

Government vs. industry responsibility

A consultant responded that managements were usually willing to assume some responsibility for the aged, but that they require a great deal of flexibility because each company and each industry has to cope with its own specialized problems of price, productivity, competition, etc. Therefore, the Federal government must establish a "broad base," with private industrial pensions providing supplementary benefits.

A union representative commented that the retirement problem of a "grocery clerk," not touched by the pension plans of large industrial establishments, was just as important as, for example, the problem of a garment worker. The government was the logical agency to provide a plan to cover all types of workers.

Referring to the broader implications of this statement, a professor asked whether this meant that the government should be expected to pay unorganized workers retirement benefits equal to those which unionized workers obtained through collective bargaining.

A consultant replied that the minimum needs of the worker should be determined and that the government should provide for these basic needs. He felt that other countries, such as Sweden, were far ahead of the United States in this respect. A union representative added that his union has many small shops under contract and that it was not fair to deprive workers in these shops of pensions merely because they did not happen to be employed in larger companies.

Suggesting that conditions of work in a "grocery store" may be sufficiently attractive to induce a grocery clerk to stay there and not to move to a steel mill, for example, where an employee does get a pension, a consultant asked whether a grocery clerk may not customarily save more money than a steel worker and thus be more adequately prepared for old age. An employer thought that this was an unrealistic assumption and indicated that in the present economy a worker cannot move readily to the place where he can make the best bargain for himself. He was convinced that the only way to get uniform, adequate pension benefits was through a government program.

A professor added that if the government, in an effort to solve certain problems, makes it impossible for a man to solve his own problems because the value of his "private" pensions (saving etc.) become depreciated, then the government also will have to assume responsibility for assistance in these other problems.

Another professor indicated agreement with an earlier statement that management's responsibility will differ from industry to industry, and feared that if the desired degree of uniformity is to be obtained through the government the entire economy will soon become hamstrung by government intervention.

Since veterans now receive pensions at age 65, and since there are indications that a large portion of the population will eventually be veterans, a government man pointed out, it is quite possible that ultimately pension benefits may flow largely from that source. As a side remark, he stressed his conviction that there should be periodic reviews of the status of persons eligible for government pensions, because some persons might get more than adequate benefits by drawing from several sources, while others receive benefits inadequate to their needs.

A union man said that corporations should supplement the minimum social security benefits by industrial pensions on an "ability-to-pay" basis, which would mean that these supplementary benefits would vary from corporation to corporation, depending on the particular circumstances. He felt it was a question, not of applying abstract theories, but of adapting to the realities of collective bargaining. An employer comment was to the effect that some corporations could pay as much as three times what others could pay towards these "supplementary benefits." The union man conceded this point, and added that this merely pointed up the fact that labor was not now receiving as much as it ultimately hoped to obtain.

One participant noted that the courts have considered pensions to be "wages" and that under the Taft-Hartley Act wages can be paid only for work performed. Since a pension, in a sense, is payment for non-performance of work, he wondered what could be the basis for any claim that management was responsibile for workers in their old age. There was certainly no "legal" responsibility, he felt.

Another person replied that the idea of management's social responsibility comes from society as a whole. Added to this are the pressures of government and collective bargaining. Although many social pressures also force the worker to provide for himself before reaching old age, he may be loath to do much about this at an early stage in his life -- a phenomenon which the speaker called the "time discount factor."

The original questionner then asked how the worker's unwillingness to provide for his own future had been transformed into a "social responsibility" on the part of industry. A professor suggested the principle might be that if in fact a man does not receive enough to provide for his future, then he is not getting enough. Another professor added that as long as there is no "saving wage" the employer has the responsibility to provide for the worker's retirement. In answer to a request for a definition of a "saving wage," he replied that this was a purely technical problem to be answered by research. One participant suggested that a "saving wage" assumed a constant standard of living. Another person wondered whether a "saving wage" could be squared with the problem of increasing productivity.

The presence or absence of a "social responsibility," said a professor, was largely a function of the size of the group involved. Thus, unemployment became a "social responsibility" only during the depression when there were many millions unemployed.

2\. The Place of Industrial Pensions in a Total Social Security Program and in the National Economy

Chairman: Wilbur J. Cohen
Social Security Administration

The chairman called attention to the following four questions on the conference agenda for consideration at this session: 1) Is there room for both private pensions and Federal insurance? 2) What are the implications of these programs for a war-geared economy? 3) What are the long-run implications of these programs for the national economy? and 4) Are any changes necessary in Federal legislation?

He suggested that the group attempt to reach agreement on some general principles relating to the respective roles of private and public plans. Such questions as the following would be relevant: Can either type of plan be made to do the job alone? On the assumption that both private and public plans are here to stay, what adjustments need be made to coordinate and simplify the two systems?

Objectives of private plans

Inasmuch as private plans were the forerunners the chairman suggested that discussion first be directed to the objectives of these plans. As background he noted that at the time the Federal Social Security program was being formulated many managements and industries having their own private plans tried to get exempted from coverage under the new national program. On the other hand, the report of the Steel Industry Fact-Finding Board (dated September 10, 1949), as he interpreted it, did not hold the industry responsible for total maintenance of the aged, but only for having some kind of adequate private plan to supplement the basic public program. What then were some of the objectives of the early private plans?

An employer asserted that the primary objective of a plan is to provide an income for the individual when his employment has ceased. In addition managements hoped that a pension plan would help them obtain and keep a better work force. In reply to the chairman's query whether the actual results had justified the expectations, he added that in general he felt that managements to some extent had attained their objectives.

A consultant cited the experience of a town of 50,000 in New York State where four out of five companies providing employment for the community had pension programs. The fifth company had come to his firm for help in setting up a retirement plan in order to compete with the other companies which were attracting a better working force. Wages and other factors in the situation were equal.

The chairman asked whether other reasons for initiating a plan might be: to make jobs available for younger men, to meet a recognized social responsibility, or something similar.

One employer was disinclined to think that his company had given much thought to the "social responsibility" aspect of the problem.

Stressing an "economic" motive, a consultant reported that studies have shown that pension plans, which permit retirement of people over 65 who are inefficient or at least less productive than formerly, will effect a sufficient saving to the company to help pay for themselves. There is a "general feeling," he said, that pensions do retire superannuated and inefficient men in the work force, although he was in no position to judge how "adequate" a job they do in this respect.

Another consultant wondered whether some feeling of "social responsibility" might not in fact be involved. He pointed to the fact that many banks had started plans as early as 1898 and that in his opinion there was no particular evidence to indicate that these plans had been started for any of the various economic reasons. These employers seemed to want to do something in the way of meeting a social responsibility to their older employees who had given long years of service. He did not feel it was a question of wanting to get rid of old employees, but rather of a general feeling of social responsibility towards these older people. He said that in his opinion collective bargaining often merely writes into a contract programs which would have been developed in any case.

When the chairman asked whether an employer's desire to keep skilled men is an important objective of pension programs, the consultant replied that all economic motives are of some significance and the desire to retain skilled workers is undoubtedly a factor, although not the only factor.

Another consultant cited cases in the Detroit area where he felt that pension plans were important factors in holding employees to their jobs, and indicated he would place more emphasis on economic motives than on any sense of social responsibility.

The chairman then asked whether this rationale for private plans in terms of their impact on employee mobility is likely to hold for the next 10-year period. Someone suggested that the role of seniority in restricting labor mobility should also be considered. A labor representative cited experience on the railroads as evidence that mobility is affected by these factors. An employer noted that his company was counting heavily on its seniority and pension program to keep employees in one of its plants from going over to a new competitor who can offer more attractive working conditions. The discussion around this point also gave recognition to other relevant factors such as the degree of home ownership, income levels, and the existence of vesting rights in the pension plans.

There was no general agreement on the possible effect a vesting provision might have on mobility. Some members of the group thought vesting could help reduce turnover if supplemented by an enlightened personnel program designed generally to keep men on the job. Others felt that vesting might make men more inclined to move around since they can thus take their pension rights along with them. One labor representative insisted that his experience with union members had amply indicated wage rates and seniority to be much more important influences than any kind of pension program on workers' decisions to leave or remain at a given plant.

At this point the chairman suggested the group at least appeared to be agreed that it was difficult to appraise quantitatively the impact of any pension program, and that factors other than pensions -- such as home ownership, wages and seniority -- have a bearing on whether employees stay or leave the employ of a particular firm. This led to further discussion as to whether these other factors, as well, had much real effect on mobility. The chairman pointed to statistics indicating a much greater degree of labor mobility previous to the last war than commonly recognized. Although a good deal of this mobility was among younger men -- below age 40 -- who were attempting to find a place to settle, it was also common to find a fairly high degree of mobility in the higher age group.

The government's role

The chairman directed the group's attention to the "three layer cake" analogy: the first layer being minimum subsistence; the second layer providing a more adequate standard supplemental to minimum subsistence; and the third "luxury" layer being primarily a function of what the individual can do for himself. There appeared to be general agreement that the function of the public program was to provide minimum subsistence. While the minimum level was not defined by the group, a professor cited some figures on current costs of the Social Security program which, in his opinion, suggested that a higher level than the current minimum was probably not obtainable.

Raising the question whether the government should assume the entire responsibility for a pension program, the chairman contrasted

Professor Slichter's affirmative answer on this question to the view of others who felt that there was a definite place for industrial pensions.

A labor representative said he thought that programs supplemental to the basic governmental program should be provided by industries where financially feasible. A consultant noted that if it is desirable to gear a pension program to the individual the three layer cake analogy is entirely appropriate. Others in the group seemed to agree that the analogy did accurately reflect the differing roles of public, industry and individual efforts to meet various levels of retirement benefits.

A consultant pointed out that any attempt to shift the focus of the public program from a minimum subsistence level to a level of more adequate over-all coverage would have to meet three basic problems: 1) the problem of cost; 2) the problem of "incentives"; and 3) the problem of gearing the agreed-upon level to the constantly rising standards of adequacy.

A union man said that a closely related problem of adjusting a plan to shifting price levels confronts both private as well as public plans, and that it would probably be easier to handle this problem under "one big plan" rather than under a great many small plans. In the consultant's view, however, the impact of price level changes was different in the two cases because the government, in the one case, would be involved in keeping the plan in operation thus raising the issue of taxation, whereas the situation is quite different for private plans. A university professor observed that costs in both cases were defrayed from the same sources -- business management and the workers. He saw the main distinction between the two types of plans largely as one of administration.

The chairman commented that part of the rationale given in Congress for not authorizing a government subsidy to the old-age and survivors insurance program was that the law did not have universal coverage. The argument was made in Congress that a government subsidy could be justified only if all persons in the population were covered by the insurance system.

A question was asked as to whether at the start of its program the government made a contribution to help defray the pension costs due to past service credit. A professor stated that although originally there had been provision for the government to make up any deficit in the program from 1943 to 1950 this provision was removed in the 1950 amendments, so that the government now considers the program as self-supporting.

A consultant observed that just as the government cannot be expected to assume the complete burden, private plans also cannot do the entire job alone, since a great many employees could not be covered. In his opinion, government and private plan benefits together should provide the older worker with sufficient income to permit him to continue approximately the same standard of living he had maintained while working, it being understood that aged people usually do not have dependent children and probably require less money for clothing, recreation, and the like.

Pension costs as percentage of payroll

The chairman declared that with an interest rate at 2% of 2 1/2% an adequate system of pensions would cost at least 14% of payroll including social security. He cited the railroad retirement system which at a 2 1/2% interest rate required about 14 or 15% of payroll. There was some objection from the participants that this estimate was too high. One person suggested that eventually lowered administrative costs would result if the government assumed the total responsibility for pensions. In reply the chairman explained there were individual differences among employers as to the percentage of payroll required for pensions. The method of financing a pension was an important variable.

One consultant said that 5% of payroll (exclusive of social security) set aside for a worker at age 25 would provide him with an adequate pension at retirement age. Other participants cited instances where adequately financed plans cost between 5% and 8% of payroll (exclusive of social security). It was pointed out that many cost differences were due to differences in accrued past-service liability, and also that to a certain extent today social security helps an employer who is starting an industrial pension plan to defray accrued liability.

A professor stated that at present less than 30% of the population is covered by social security in this country, and that it will probably be 1980 before even 50% is covered. While this would cost only 6% of payroll, the costs would rise much more if the total population were covered. The chairman indicated that only eight or nine million people are currently covered by industrial pension plans instituted either unilaterally or through collective bargaining. Several participants were inclined to feel the two sets of figures just presented were evidence that there was ample room for expansion of both private and government programs.

Possibilities of simplification

The chairman asked the group to consider the possibility of coordination and simplification of existing plans, which he thought were often so complex that employees rarely understood their intricacies. The discussion produced further testimony to the complexities of both private plans and the government program but little hope that simplification to facilitate understanding would be possible. A consultant contended that attempts to simplify complex problems are undesirable and that current publicity devoted to collective bargaining negotiations on pension issues had treated these issues far too superficially.

"Flat benefits"

A comment by one participant that he had heard of a "simplified" flat-payment plan providing $50 monthly benefits to everybody touched off a general discussion on the subject of "flat benefits." A government man pointed out that if pension benefits are not tied to past earnings Congress can have no effective test for determining what benefits should be paid at a given time. He added that use of a flat payment would necessitate the abolition of the payroll tax and the substitution of payment out of general tax funds.

A professor objected to the huge cost of such a system of flat benefit payments which would amount to $7.5 billions annually for pensions of $50 per month -- a very heavy burden on the nation. A consultant reported that Sweden provides flat payment benefits for minimum subsistence, and that additional supplementary benefits are based upon wages. He thought such a system would not be undesirable in this country. A government man stated that unless the flat payments were paid from an ear-marked tax fund there would be no guarantee of continuing payment, and that some degree of assurance of continuance of payment, such as now exists in this country, was better than none.

Another consultant suggested that a flat payment which was not based on a means test might eliminate the cost of administering such a means test and thus lower total costs. A professor repeated his objection to "the huge cost" of such a system which he termed "highly unrealistic," since the present system covers only 24% of the population and provides average monthly payments of <u>less</u> than $50 per month. This showed what it would cost if a benefit of <u>at least</u> $100 were extended to 100 million people. He assumed that a pure "hand out" was undesirable, and pointed out that Sweden did not have a "hand out" but, rather, a system of assistance on a means test basis.

Another professor thought that a comparison between the U. S. and Sweden was misleading since Sweden had a generally increasing rate of productivity combined with a decreasing population, which is not the case of the United States. He added that it was contrary to all "sound" pension principles to give "X" amount in benefit payments to workers without tying the payments to something substantial.

A government man said that when the amended social security act was being considered in the Senate Finance Committee a provision calling for a minimum flat payment for subsistence was dropped on the grounds that it would be subject to considerable political pressure and manipulation. A lower minimum benefit might be needed in the South than the North, causing friction between these political groups. He denied the accuracy of the belief that a fixed benefit system would result in considerably reduced administrative costs.

A professor pointed out that a $20 minimum payment exists in the present law but that not everyone is covered and that among those nominally covered not everyone is eligible for this minimum benefit. Someone then suggested that the first subsistence "layer" might be provided completely from general taxes while the second "layer" could be financed by contributions and payroll taxes.

An employer interjected his opinion that <u>any</u> "hand out approach" would "pyramid" and be harmful to the economy. A labor representative also expressed opposition to complete assumption by government of the financial responsibility for pensions, and added that a worker should participate in the financing of any retirement program so as to have a genuine stake in the plan.

<u>Impact of pension plans on investment</u>

Turning the discussion to the impact of both public and private pension programs on the economy in general and on the investment picture in particular, the chairman informed the group that at the end of 1950 the reserves of private plans were around 7 billion dollars and that the net annual accumulation is between one and 1.2 billion dollars per year, with the possibility that this rate of accumulation may increase. Accumulation was defined as the net amount of accrual of funds in the plan -- that is, the difference between everything taken in and everything paid out during the year. Latest information (as of the end of 1950) showed total reserves in both private and public plans (including coverage of teachers, railroad employees, and all others) to approximate 30 billion dollars. Roughly 13 1/2 billion dollars was in OASI, about 2 billion dollars in the Railroad Retirement System, 7 billion dollars in private retirement plans, approximately 4 billion dollars in state and local plans, and close to 4 billion dollars in other government retirement programs.

A professor pointed out that, although the data were not conclusive, he thought employers were currently investing in private plans roughly as much as or perhaps slightly more than in OASI. There are now about 2 million old people now on OASI rolls but only 200,000 receiving industrial pensions.

Calling attention to the relationship between these reserves and investments the chairman noted that the Sears and Roebuck pension fund now owns approximately 20% of the company's corporate stock, a phenomenon suggesting several possible interesting developments. For example, there is a possibility that pension plan trustees might at some time invest their funds in the stock of competitors. Pointing to the one billion dollar A.T. & T. fund, and the General Electric fund of one-half billion, the chairman wondered whether anyone had any fear of the effect on investment of the accumulation of such huge funds.

A consultant replied that in the investment field there was a considerable difference of opinion over this matter, but that he thought these funds at the present time are providing a "cushion" in the investment market thus tending to make the market more stable. An entirely new source of equity market funds is being created, because pension funds, invested as they are in the "blue chip" type of securities, tend to push risk capital out of the market for this type of security and force it into other more appropriate areas -- namely, true risk ventures and equity capital for smaller types of businesses.

In answer to the question whether these funds might not result in a slight inflationary pressure, the consultant indicated that, while this was a possibility, they can also have anti-inflationary effects. In addition, it was his opinion that any future break in the market could never reach the serious proportions of the 1930's, because so many current investments are not speculative but are more appropriately described as being in "deep-freeze."

Investment of pension funds in common stock

In answer to a further question as to whether there was any difficulty in finding good investments for these funds, the consultant went on to state that whereas, in the past, trustees of pension funds never wanted to invest their funds in common stock, they are now doing so for two reasons: 1) because it reduces the cost of the plan over the years; and 2) because it is the only way in which they can share in the profits of some of the stronger firms.

Someone commented that while such a trend may allay fears that equity capital is drying up, he still feels that it may be slightly inflationary. The consultant restated his position that the effect was not necessarily inflationary, and added that a new source of equity capital was being developed which would tend to spur production, since new firms would find capital available when needed.

Another participant was more inclined to emphasize the risk involved in investing in common stock and the possible impact this practice could have on such matters as accumulation, concentration of ownership, and investment in competitive enterprises.

It was noted that many states were now amending their laws to permit investments of these funds in common stock, and there was a comment to the effect that this practice might call for the development of safeguards against various risks involved.

The consultant who was defending the practice admitted there was a risk involved in such investments during a period of depression or a declining economy, since investors usually became afraid and sold their stocks, thus inducing a general fall in prices of stock. However, he felt that <u>if</u> the holders of stock could be induced <u>not</u> to sell but to hold on, they would get a good stable price for their stock over the long run.

Subsequent discussion showed many of the participants felt this last supposition to be unrealistic, and that many plans, having invested heavily in common stocks, would find themselves in very perilous circumstances in the event of a depression. Several persons testified to the reluctance which union leaders have shown in the past to investing accumulated funds in anything but government securities, an indication it is unlikely that trustees of the currently negotiated funds would be inclined toward investment in common stocks.

The consultant replied that while this was largely true in the past and still to some extent at present, he felt unions were coming gradually to look more favorably upon other types of security than government bonds. He attributed the past fear of common stocks to the fact that union trustees of these funds were inexperienced in the investment field and were unsure of the speculative element involved. He also attributed it to the general nature of a union with its particular type of internal politics, where officers given responsibility over such matters as investment of funds had only short tenure of office.

<u>Pension plans in small or marginal firms</u>

At this point the discussion turned to a consideration of the general effect the current pension drive might have on marginal firms and all types of smaller businesses. It was noted that for firms in the steel industry where the burden of a pension plan seemed too great, the union had made exceptions to its general pension program and had taken a wage increase or some other benefit more in line with the particular company's "ability to pay." It was also pointed out that a wide diversity of types of plans exists within the industry itself.

The chairman asked if anyone felt there was some definite limit on the feasibility developing pension programs for smaller businesses and, perhaps, less profitable firms. A consultant replied that he has found it possible to provide many small plants with a "reduced" pension plan based on their ability to pay and that such a plan in conjunction, possibly, with a supplementary profit-sharing plan will prove very satisfactory. He added that a "fair" profit-sharing formula may enable workers to obtain even higher total benefits than in companies where a larger base permits a more ample pension formula.

Another consultant agreed with this and stated that there also were many cases where a smaller pension formula in addition to old age and survivor's insurance could bring the pensioner a greater total benefit than many of the "over-all" formulas (i.e. a certain amount inclusive of social security) at some of the larger companies.

While a third consultant contended there were few firms so unprofitable that some kind of a pension program would not be possible, another participant warned it would be incorrect to assume that all the firms which can financially support a pension program will necessarily want to establish one. To this a government man responded that in the long run he thought a situation would be reached where all the plants in which it was possible to have plans would have them while the plants without plans would be financially unable to develop them -- a sort of "half-slave, half-free" arrangement. Further comment from the group suggested that the long run picture could depend, among other factors, 1) on the future extent of the unionization of currently non-unionized sectors of the economy and union policy for these sectors when organized, and 2) on the entire "complex" of bargaining and competitive relationships. One participant observed that the ultimate result would probably be about the same as for any other variable which might be introduced into the situation. Wherever some variable enters the picture to make it difficult for marginal firms to compete, these firms must either come up to the standard or get out of the industry.

Manpower problems

The group turned again to the topic of the effect of pensions on labor mobility discussed in the earlier session. In the discussion, wage rates and seniority were stressed as factors probably having a greater effect than pensions on reducing turnover in plants. It was noted, however, that younger workers tend to be more mobile than older and to be attracted by higher wage rates and opportunities for advancement, whereas seniority provisions and pension plans tend to hold down the mobility of older workers.

The chairman then asked the participants to consider the effect of seniority and pensions upon manpower problems in a defense-oriented economy under wage controls. He pointed out it would be necessary to draw skilled labor from one plant to another with higher defense priority and asked how the shifted workers' pension and seniority rights could be handled. Several participants were inclined to believe that wage differentials would be used, as in the last war, to induce labor to move from one plant or area to another, and that these might be effective.

An employer commented that under a defense economy some plants which were forced to curtail production would give leaves of absence to their workers to permit them to work in more essential industries while preserving their seniority and pension rights. A government man noted that the impact of increasingly higher taxes was to make immediate higher wages more important to workers than the long-run attraction of pension benefits.

A consultant described the labor force as more "rigid" now than ever before and suggested public policy would emphasize "bringing the job to the worker" in place of "bringing the worker to the job," the approach used during the last war. On this point one participant commented that such an approach might introduce other "strategic" problems. For example, it might interfere with a policy calling for the dispersal of critical industrial areas.

Another participant reported a well-known economist had asserted in an article that voluntary methods of meeting manpower needs had cost too much during the last war and that methods close to compulsion should be used this time.

Impact of pension costs on industry

The chairman suggested that the group consider the impact of pension costs on the "business enterprise." One person responded that costs of pension plans may put too great a burden on the consumer, to whom the costs are ultimately passed on. Public utilities, he noted, supported plans costing between 5% and 10% of payroll whereas the cost in the more competitive industries has generally been between 3% and 5% of payroll. He asked whether this suggested that the consumer is being unduly exploited in the public utilities industry. Another participant commented that higher pension costs in this industry may be due to the fact that public utilities are large and old industries with more past service credits to fund.

Another person remarked that some industries have higher costs than others because they attempt to fund past service credits in a shorter period of time. For instance, the cost was high in the oil industry because they attempt to fund past service credits in a shorter period of time. For instance, the cost was high in the oil industry because that industry's plans provided for complete funding of past and present credits within ten years.

Impact of taxation on pension plans

The chairman raised the question whether the impact of taxes would have any effect on the method of financing plans.

One consultant replied that increased personal income taxes would discourage "contributory" plans because such taxes made it more difficult for individual workers to contribute to the pension plan, while increased corporation taxes would have the effect of encouraging "non-contributory" plans because of the greater tax credits made possible.

New plans would then probably be non-contributory and old contributory plans may have to be changed. He added that the wage freeze would also have an effect upon future plans because pensions are considered as wages.

A union man said he felt that even under wage stabilization there would be opportunity to correct wage inequities through pension plans. A consultant replied he thought other serious inequities would result from such an approach. For example, a firm operating under the excess profits tax would find it possible to expand its pension program while a firm in the same labor market but not under the excess profits tax would be "caught in a squeeze," since it would not be able to grant higher pensions (as a substitute for wage increases) and thus be ineffectual in its efforts to maintain its labor force or attract needed workers.

3. . . . . Practical Factors to be Taken Into Account in Connection With Pensions

Chairman: Edwin E. Witte,
University of Wisconsin

In opening the session the chairman noted that the topic "practical factors" could be viewed in three different ways. First, from the employer's point of view, the "practical" problem would consist in keeping costs down. Many firms, moreover, would want the government to assume a good part of the job. Second, from the union point of view, the problem is to obtain as adequate a pension as possible, with little direct concern over cost. Third, from the public and the public-interest point of view, the concern would be with both of the above aspects of the problem, perhaps with a slightly broader focus and outlook.

The role of industrial pensions

To provide a background for a discussion of practical problems, the chairman suggested that a brief summary of the "general philosophy" of pensions would be helpful. He pointed out that industrial pensions cannot be a substitute for OASI which, in turn, can only aim at a reasonable subsistence standard. No public insurance program in the world, he asserted, will ever be able to provide more than minimum subsistence -- a standard which is still far from attainment for the total population. Industrial pensions can never do the entire job since a large percentage of the aged are women of whom many are unable to work. Also, only a small percentage of the persons covered by plans at any specific time ever actually receive pension benefits. Thus, industrial pensions can never serve more than a small segment even of the working force. Moreover, retirement benefits alone do not meet the total old age problem. In addition there is need for extending rather than contracting the average length of the working period of life and for maintaining a high level of production and productivity.

The chairman considered that industrial pensions have three principal roles. In the first place they constitute a discharge of the obligation an employer may feel toward his superannuated employees who have been with the firm a long time. In the second place, an industrial pension can provide a supplemental source of income beyond minimum subsistence. Thirdly, industrial pension programs contribute to the improvement of labor-management relations. Amplifying this third point, the chairman suggested that the very process whereby workers and employers jointly tackle the serious problems of old age may create a community of more friendly relationships which, in turn, can make for better overall industrial relations.

Breadth of coverage

Following this background summary, the chairman suggested that "multi-unit coverage" might be the most appropriate topic to discuss first. He informed the group that about 15,000 or the great majority of current pension programs are single-unit plans. Among the better known plans not restricted to a single company is the Toledo Plan, which is not as "new" an idea as is sometimes supposed. Basically it is a "pooled" plan with a limited interchange of credits. However, there are many "employer association" plans with even broader coverage. For example, the United Mine Workers' plan is a pooled type with complete interchange of credits throughout an entire industry. He noted that the clothing workers in New York and the electrical workers also have plans providing for complete interchange of credits throughout a specific section of an industry. It was the chairman's opinion that single company plans, especially small company plans, have very serious limitations unless they contain adequate vesting provisions.

A labor representative said that his union favored a community plan in situations where it has contracts with a number of small plants, but explained it had not yet been able to put such a program into effect. He added that his union is experiencing difficulties in negotiating pension plans for their members in certain large plants where the union bargains only for a small group of skilled workers whereas the majority of the employees are members of some other union.

The chairman asked the participants what they thought would be a good solution in a situation where a number of different unions were the bargaining agents for varying sized sections of a single firm.

An employer replied that the situation often did become very complicated, but added that he still did not think the problems were very serious. He indicated that his company had contracts with several different unions and that, therefore, it was administering a number of separate pension plans, which, in fact, were not widely different from one another. In answer to a query as to the expense involved in keeping records and performing other operations for so many plans, he replied that it was expensive and inconvenient to the company and that the situation had many illogical aspects.

The chairman asked whether "associational" agreements were desirable. A consultant commented that there were two kinds of complex bargaining situations: one, like the example just given where a single large employer has the problem of meeting varying pension demands from several different unions; and the other, where "associational" type plans would make it possible for groups of small employers or employers lacking a steady work force to institute pension plans. The longshoring operations and the construction industry are examples of this latter category.

Arrangements for small firms

The chairman asked whether there were some alternative approaches to pensions (purchase of insurance, for example) which would be more feasible than the trust-fund approach for small plants. One participant said that the cost of insurance would be prohibitive for many small companies.

Another possible approach suggested was the Teachers' Insurance and Annuity Association program which provides individual retirement annuities on a non-profit basis. A consultant agreed that plans similar to the teachers' insurance program in rather wide use but that he does not consider them practical solutions to the problem. He cited the case of the Mellon Bank of Pittsburgh which offers service of this kind to a number of member banks, and other cases where employers or employee groups pool their funds in order to obtain broad coverage. In most cases, he felt, the groups desiring these pooled plans are usually not sufficiently stable for the development of a sound program. One difficulty is in getting the groups involved to participate adequately in the program. Another difficulty is in knowing at any given time exactly which and how many individuals are covered. In addition, he said, pooled plans always found it difficult to handle the problem of past credits.

The chairman quoted a recent still unpublished article by Byron L. Johnson of the University of Denver to the effect that, generally speaking, small employers could institute pension programs only with government assistance. The government would collect the contributions from various groups of these employers and administer a retirement system for them on a nation-wide basis. He said this implied a very large national insurance program and asked the participants what they thought of this suggestion.

A consultant responded that Canada had had a rather unsatisfactory experience with a program of this kind. This is its system of voluntary annuities available to all Canadian citizens on both an individual and a group basis. This was offered at 30% below the going insurance rate, which in effect constituted a government subsidy. Since this appeared to provide an opportunity for a good investment, many employers with funds free for investment tended to purchase the policies while those employers for whom the plan was originally designed -- that is, those who were unable to afford the regular insurance -- did not purchase into the program. Since the "wrong" people were buying most of the annuities, he said, the government found it necessary to raise its rates.

The chairman observed that in situations where there were a number of small government retirement funds such as those of municipalities, within states, the trend has been towards creation of an all-embracing state system to which the small units could make contributions in order to obtain the advantages of broad coverage.

A professor said that, in his opinion, most of the small plans in Illinois are actuarially unsound. For example, he asserted the University of Illinois' plan is unsound with an actuarial reserve deficiency of $20,000,000 as of August, 1950. He added that the only public plan in Illinois without an actuarial reserve deficiency is the Chicago Library plan, and that the end result of attempts of many small units to establish their own plans will only be "chaos".

A consultant suggested that despite what had been said previously against pooled plans, a possible solution would be to combine several funds in a single large program, and cited a case in West Virginia where 150 banks have pooled their funds and pro-rated the fees and expenses among the various banks within the program. Another consultant noted in connection with a similar arrangement in the state of Michigan a court had ruled that such a plan constituted in effect a pooling of mortality rates and therefore was an insurance program not entitled to function as a pension trust fund. One participant commented that the legal status of such an arrangement would probably depend upon how it was formed and how the agreement was phrased.

The chairman said the group apparently agreed that if small firms were to obtain adequate coverage under a sound pension plan a pooling arrangement or insurance provided by a commercial insurance company would provide the best answer.

One member of the group suggested that many employers might be reluctant to join in multiple-employer arrangements for fear that this would lead to industry-wide bargaining. He also noted that pooling arrangements might in effect penalize certain firms having some particular advantage which they would have to give up by joining in the "pool".

<u>Insured vs. self-insured plans</u>

Proposing that the group take up the agenda topic of "commercial insurance plans vs. self-insured plans," the chairman remarked that the choice was not limited to these two kinds of plans alone, since combinations of the two were also possible. For instance, in most of the plans of the steel companies the benefits payable to workers on retirement are insured by commercial insurance companies. It was his opinion that the conditions under which self-insurance is permitted must be rigidly controlled and that self-insurance should be restricted to strong individual firms and, possibly, associations of smaller firms. He questioned whether for the small firm self-insurance was in the interest either of the public or of the employer himself.

One participant explained that under a self-insured pension plan actuarially determined sums of money were put into a separate fund which could not be used for other purposes. A consultant noted that his firm advises employers with less than 100 employees to have an insured pension plan, and recommends the trustee-type (self-insured) plan for those with over 100 employees.

Unnecessary confusion accompanies the usual discussion of the advantages and disadvantages of the self-insured or trustee-type plans, one consultant remarked. While there may be claims that insured plans are "guaranteed," in reality they are only "guaranteed" at a given point in time, he said. In the long run a trustee-type plan also may not be cheaper than other types. The cost of a plan is not completely or accurately known until each participant retires, collects his benefits and dies. An actuary can only roughly estimate future developments and must take into account many other variables than mere administrative cost -- such, for example, as changing mortality rates, the amount of benefits, labor turnover, etc.

In the speaker's judgment, a commercially insured plan was preferable for a small firm, whereas, for a large firm the trustee-type plan was generally the more satisfactory, and for a medium-sized firm both plans were equally practicable. He said that the main factors which usually influence an employer in the selection of one type of plan or the other were: 1) the bias or advice of the particular consultant involved, 2) the type of plan business competitors have, 3) the kinds of investments considered desirable, and 4) the "trend of the times." In explanation of the last two factors, he added that commercially insured plans generally provide 2 1/2% interest while invested funds usually bring 4% interest, and that although ten years ago most pension plans were insured, almost 90% of the newly established plans are of the trustee type. He concluded that in only about 5% of the pension plans instituted today was the medium of funding selected strictly on its merits," and that the provisions of most plans were based on a "cost" approach, in which anticipated costs are the main determinants of the specific provisions of the plan.

Public regulation of retirement plans

Noting that some states have already applied some general insurance regulations to pension plans, the chairman posed the question of the need for public regulation of trustee-type plans.

An answer to this question would depend upon how many private pension plans actually fail, said one participant. A professor remarked that some regulations already exist inasmuch as the Department of Internal Revenue requires actuarial computations before tax credit will be granted. A consultant responded that there was nothing in the Internal Revenue Code requiring "actuarial soundness," since the law stipulated only that a plan be based upon an actuary's report and not that it be examined in terms of its "soundness." California legislation, however, gives the state Insurance Commissioner the right to examine certain types of pension trusts, particularly plans where individuals are trustees.

A professor recalled his experience as public member of the board of trustees of an industrial pension plan. At the beginning, funds did not accumulate very rapidly. Later, when the money did come in at the required rate, management representatives asked if benefits could be increased. He said he had to caution them that the funds were not yet sufficient even to pay for the promised benefits, let alone to make it possible to increase the amounts. He concluded that public regulation of private pension plans is necessary in order to protect the whole system from the danger of financial collapse which overtook the early fraternal insurance system.

Selection of benefits

In directing the group's attention to the topic of "benefits," the chairman contended that discussion of benefits normally cannot be separated from a discussion of costs. The "benefit" is the employee's main focus of interest, while "cost" is the employer's. Benefits could justifiably be discussed apart from costs in this instance, however, since the satisfaction derived from benefits usually determines the success or failure of a plan in the employee's mind. In other words, he thought the group might profitably discuss some of the non-cost problems involved in the selection of benefits.

A consultant related the selection of benefits to the implicit or explicit objectives of a plan. In drawing up a scale of benefits the employer and his actuary must decide what they desire to achieve by the plan. They then formulate an "ideal plan," and after the cost of this "ideal plan" has been computed, the benefits may be shaved down until the cost meets the employer's requirements. It was noted, however, that this description, strictly speaking, applies only to plans which are not negotiated through collective bargaining.

The chairman called attention to the many elements which are considered in the establishment of pension plans: eligibility, retirement age, treatment of post-retirement, type of benefits, basis for contribution into a given fund, etc. While there are an infinite variety of plans and benefits which might be developed, he asked the group whether there are any "vital concepts" relevant to drawing up a plan and setting the scale of benefits. In line with this inquiry, the consultant who had mentioned the "ideal plan" was asked how its component parts were developed.

He replied that the features of an "ideal plan" in a given situation are determined by the specific objectives of the employer, so that a plan is often integrated with an already established industrial relations program. Thus an "ideal plan" does not imply a "luxury" type plan and may very well have certain "thin" provisions, because of its being related to the specific employer's objectives.

Another consultant added that there is no single "ideal" plan. A department store, for example, might not want to set the retirement age for saleswomen as high as age 65 because under existing sales practices it is not deemed desirable to have women close to that age sit behind the perfume counter. A pension should always be adapted to the particular situation, he asserted.

The chairman hazarded the observation that adaptability was one advantage a private industrial plan had over a more uniform national government plan. On the other hand, he contended, a national program can give consideration to needs which are overlooked by an individual employer and thus can help prevent the "fragmentation" of society into small groups with differing degrees of retirement security which he viewed as a serious danger.

The question was raised as to the kind of assumptions which actuaries use in proposing specific benefits. A consultant's answer was that they were guided by two major considerations: 1) the objectives of the program, and 2) an estimate of a reasonable rate of return. One participant, currently in charge of a pension plan, contended that another major consideration is to provide a pension which will permit an individual to maintain approximately the standard of living he enjoyed prior to retirement. In general, he added, this can be accomplished by giving the pensioner 50% of his final earnings, including primary social security benefits.

A consultant pointed out, however, that many employers and employees both feel current pension benefits to be inadequate, and that more than a general "rule of thumb" is necessary as a measure of adequacy of benefits. Even 60% of an employee's 1940 earnings would not be adequate today, another consultant remarked, because of the steep rise in the price level. In drawing up benefits, he asserted, consideration must be given to the possibility of inflation and to other future conditions and long-run factors.

An employer agreed that inflation was one of the major problems in connection with benefits. A union representative suggested that partial provision for future developments can be made by setting benefits at a certain percentage of the average income for the last ten years of service.

The chairman responded that in his opinion it is impossible to do any more than promise to give what is considered an adequate pension today, since it is impossible to predict what will happen in the future with any degree of certainty. There still remains, however, the problem of determining a standard of adequacy for today.

A consultant cited one company which had tied benefits to the cost-of-living index. A union man referred to another company which, when the cost-of-living rose, had increased the benefits for those who had already retired.

Relation to Social Security benefits

Another union man declared that his union was opposed to the idea of tying industrial pensions to social security benefit increases because these increases (which, in the long run, will be responsive to rises in the cost-of-living) might gradually eliminate private industrial pensions altogether. One unionist added that the "three layer cake" analogy logically implied that industrial pensions should not be tied to social security inasmuch as the latter was designed only to provide basic subsistence.

A consultant asserted that the size of the "second layer" should be closely related to the "first layer." The fact that the size of the "first layer" may rise in response to the rise in the cost-of-living does not imply elimination or reduction in the size of the "second layer." However, he added, it might be necessary to investigate the proportionate adequacy of the "second layer" in relation to the first, and this might lead to a decision to increase the size of the "second layer" as well.

This principle was not followed by certain corporations, the chairman said, when the benefits in the Federal old age insurance system were raised in 1950. Some corporations cut the benefits under their private plans to the extent of the increased OASI benefits under the amended social security act of 1950. In this situation, he indicated, it was the corporation and not the employees who benefited from the increase in social security payments -- a fact which created a high degree of ill-will among the employees. This policy, fortunately, was not general but was quite unjustifiable.

A consultant pointed to a NICB survey showing that most corporations were not cutting their private pension benefits as a result of increased social security benefits. He feared this increase in percentage of payroll set aside for welfare purposes might have a deleterious effect upon the price structure since employers will tend to pass the added costs on the consumer in a "spotty fashion," depending upon their own particular situations. This was the reason, a government man declared, for his opinion that a percentage of payroll provided a realistic basis for computing costs -- because the economic effects of increased benefits could be foreseen.

A labor representative asserted that increased welfare costs do not necessarily mean increased production costs, and suggested that some employers can easily cut some of their profits without damaging their economic positions.

Inflation and pension plans

A professor described inflation as the "worst enemy" of pension plans because even "actuarially sound" plans can easily be undermined by inflation. He wondered whether unions had paid much attention to this problem. A union man replied that labor has come to the point where, in his opinion, it will have to reexamine its wage policies in terms of their inflationary effects upon the economy. Unions, he said, formerly helped to redistribute the nation's earnings. This had good effects, but now their policies may encourage inflationary tendencies. The answer to inflation, he felt, could be found in added productivity and lower prices, but he added that labor is not strong enough to bring down prices at this time. There was a comment by the chairman that the problem of inflation had its origin in the tremendous increase of money in relation to goods produced.

A government man stated the public program should assume the responsibility for revising pension benefits in the light of the inflationary rise in the price level, because it was in a position to make these adjustments more readily than the private industrial plans. A professor noted, however, that some corporations do make these adjustments, and a labor representative added that the government man's proposal might lead to a form of subsidization. Another professor pointed out that it had taken the government fifteen years to revise the old social security benefit scale and that meanwhile people had had to make adjustments to changed living costs. An employer said he felt the government should be urged to make every effort to curb inflation through such means as tighter control of credit, increased taxation, and restriction of government expenditures.

The chairman remarked that, unfortunately, a great many people get a pleasureful, "giddy" feeling from inflation and have little realization of the harm it can do. The people receiving pensions are the ones immediately hurt by inflation, but they have little influence on inflationary trends. In summary, he asserted there seemed to be a concensus of the group that inflation was the "number one enemy" of both public and private pension programs.

4. . . . . Financing Factors to be Taken Into Account in Connection With Pensions

Chairman: Maurice Wolfman
Actuary, Chicago

Vesting

At the request of several participants, the chairman led the group into a discussion of vesting rights in pension plans. A union representative said he did not believe any company or any union, through an agreement, had the right to deny to a departing employee the money which had been put aside for his pension. In his opinion, a pension plan without vesting rights was not a true pension plan.

This point was amplified by a university professor who noted that pensions, as well as other "fringe" benefits, are, in effect, wage payments in one form or another, and, therefore, constitute compensation for service rendered which it would appear an employee has the right to take with him if he moves. He suggested that vesting may perform an important function as an aid to an unemployed worker in finding new employment, thereby increasing his mobility.

Inasmuch as vesting is an expensive feature of any plan, a consultant asserted that although he favored vesting he thought it should not become effective immediately. After 10, 15 or 20 years of employment an employee has in a sense "paid his way" and could then become entitled to some vesting privileges. Short of such a period, however, vesting may be uneconomical, and the money paid into the fund for short-term workers can be counted on to help defray the cost for the others who do stay long enough to draw their pension benefits. He felt it was difficult to anticipate the effects of vesting in a given firm. The effect could be very serious in a particular case if a large percentage of employees with vesting rights were to leave the company over the years. He thought of vesting primarily as deferred income and not as cash, and felt that normally vesting discourages rather than encourages mobility of employees.

The chairman pointed to a possible inference from this reasoning: that employee mobility might be greater during the period before vesting becomes effective.

A government man wondered whether the fact of a worker having vesting rights in the plans of several companies could have any effect on the liklihood of his continuing to work after retirement age. One participant felt this would depend on the total amount of the pension, while another thought a worker might be less inclined to work after age 65. In the subsequent discussion several members of the group were of the opinion that for economic and psychological reasons a worker who received a number of small pension benefits from several companies would be more likely to continue working than a worker who received a substantial pension from a single firm. The thought was that such a situation made it attractive for a worker to continue on at his latest employment upon turning 65 while becoming eligible to receive additional income accruing from pension rights arising out of previous employment.

A unionist contented that if the purpose of pensions is to help aged people, full vesting is necessary, but that if the purpose of pensions is to try to tie a man to his job, other kinds of an arrangement might be justified. In answer to a question from the chairman about the effect of vesting upon hiring practices, the unionist replied that an employer would not hesitate to hire older workers if they had vesting rights coming to them from some other company, and that this was a very important argument in favor of full vesting. A professor, on the other hand, thought that employers would still be as unwilling to hire men beyond 40 as they always had been. In reply to the unionist's contention that this reluctance on the employers' part was due to high insurance costs, he suggested that encouraging employers to hire older workers was a complex problem which involved pointing out how a company can afford to hire these older workers as well as convincing employers how it is to their advantage to hire them.

Another unionist pointed to the experience of a company whose plan did not have vesting but where the turnover among young workers created a serious problem. He felt that vesting might provide a solution to this kind of problem, since the worker could see, year by year, he was building up his rights in a pension program and thus would gain a definite sense of accomplishment. A worker who can see his security slowly growing would be more inclined to stay on his job. He added, however, that he did not favor allowing employees to take their money out with them in cash, but was in favor of vesting rights only as deferred income. Another union man emphasized his agreement with last point, adding that in his opinion the whole purpose of a pension plan was violated if employees could take their money out in cash, in which case it would have been preferable to give them the money in the first place.

A consultant suggested that a major problem was the tendency for the individual employee, as he builds up assets on his balance sheet in the pension program, to feel less inclined to take action on his own to protect himself for old age. When he sees his assets being built up in a pension fund, he may alter his pattern of saving and tend to view these assets in a different light, especially in times of depression. In this way vesting may have the effect of negating the one primary purpose of a pension plan -- protection of the worker in his old age.

In reply to an employer who asked what should be done about this tendency, the consultant confessed his uncertainty. He knew that many companies were having unfortunate experiences with vesting provisions because of the funds being drawn out, making administration of the pension program more difficult. A possible solution might be to restrict use of the funds solely to the retirement purpose for which they were accumulated.

Someone asked whether the advantages of vesting were affected by the contributory or non-contributory aspect of financing pension plans. Although one participant felt that only in a contributory plan did an employee have a clear and definite right to at least that part of the fund he had built up, several others who entered the discussion were of the opinion that the distinction between the two types made no real difference in the way employees feel either toward their "rights" in the total fund or toward the inclusion of vesting provisions. One member of the group said that even in the case of a non-contributory plan he could envisage the possibility of "raids" on the funds by workers who under certain exigent circumstances would lay claim to the money.

A consultant responded that in his opinion fund-raiders were "straw men," and that he favored vesting because it helped make industrial pensions do their essential job -- that of providing the necessary "second layer" of retirement benefits. He felt that if industrial pensions could not do this job, labor would try to get the government to take on the responsibility for this so-called second layer -- a development he did not consider desirable.

An employer asserted that he was strongly in favor of vesting at as early a date as is practicable. In his opinion a company should not withold vesting rights in an attempt to induce employees to stay on the job. This is based, he said, on his fundamental belief in a free labor force and a free enterprise system. It was his feeling that in the earlier discussion on labor mobility there was too much emphasis placed on ways and means of impeding mobility. On the contrary, workers should be as free to move around as possible. A properly balanced pension program with vesting provisions could help maintain the conditions for freedom of movement and choice of work.

Permanent disability provisions

The chairman directed the attention of the group to the issue of whether or not permanent disability benefits should be included in pension plans. This was related to the subject of vesting, he said, by raising the question of the amount of equity in a pension plan a worker will have if he should become permanently disabled before reaching retirement age.

There was considerable difference of opinion in the group over the best approach to this problem. A professor felt that the two problems -- the problem of the aged and the problem of the permanently disabled -- were quite different from one another and required independent consideration.

A government man suggested that OASI was the logical agency to assume responsibility for the permanently disabled, a proposal which was objected to by an employer on the ground that administration of a disability benefits program on a national level would be undermined by "graft" and illegitimate claims. The employer felt some doctors would be tempted to give fraudulent certificates of disability and, therefore, any program covering the permanently disabled should be handled on the "local level" in small units where it could be more effectively policed.

Expressing agreement with this latter position, a professor pointed out that the problem of permanent disability was much more difficult to handle on the national level than the problem of retirement. Another major difficulty was related to the fact that actuaries were not able accurately to estimate the cost of such a program. The first step toward doing something about permanent disability, therefore, is collection of data essential to such estimation of cost.

The chairman observed the experience of most insurance companies with permanent disability programs has not been satisfactory. The difficulty lies not so much in the collection of actuarial data, as in the administration of such a program. Under some experimental programs a worker who became permanently disabled after age 50 was paid disability benefits between the date of disability and the date of normal retirement, after which he became eligible to the regular annuities based on accrued service.

The government man explained that he felt a Federal program giving minimum subsistence benefits to the permanently disabled would be preferable to private industry plans because Federal benefits could be geared to previous wages and length of service. A recent study of the Rhode Island diability program was cited by a consultant as indicating that a major problem in such a program arises from the difficulty in distinguishing between total disability and partial disability. In reply, the government man pointed out that by gearing benefits to wages malingering could be prevented and some administrative difficulties could be alleviated. While this might prevent malingering, observed an employer, it could hardly provide adequate benefits for workers who were really permanently disabled -- a comment to which the government man replied that one cannot "have one's cake and eat it too," and that some assistance was better than none.

Other participants showed some concern over the problem of "malingering," one person noting that a Canadian study showed "malingerers" constituted 3% of the claimants. Another member of the group tended to discount this problem, however, asserting that most permanent disabilities are medically verifiable. He conceded, nevertheless, that in the case of commercially insured programs management itself often added to the pressure for payment of benefits to "malingerers."

A professor described the early disability programs drawn up by insurance companies as unsound largely because of the lack of adequate data, but added that there were a few good plans in existence today. A union man wondered why insurance companies were opposed to the government entering this field, since they are apparently in general unwilling to write group disability insurance. The chairman observed that while some insurance companies did write "individual" disability policies, they did not cover the entire span of an individual's life.

In the further discussion around this general topic of permanent disability the observation was made that a typical plan, which provides disability benefits after age 50, might raise the total cost of the entire pension-disability program to 12% of payroll. This elicited a comment that such a plan could not begin to meet the disability problem because most of the accidents which create the problem occur before age 50.

Summarizing the discussion on this topic, the chairman noted agreement among the participants that administration was the major problem of any permanent disability benefit program. The group also appreciated the serious inadequacy of current data for the second establishment of such a program.

Funding vs. pay-as-you-go

The chairman asked the group to consider the factors which may determine the selection of a funded or a pay-as-you-go pension plan. To a remark that this choice often seemed to depend on "how the wind was blowing in the collective bargaining situation," the chairman responded that he felt that the problem went deeper than this and that it had existed long before collective bargaining entered the picture.

Most of the very early pension plans were on a pay-as-you-go basis, a professor asserted, but they ran into many difficulties which ultimately led to failure. A consultant pointed out that from the employer's viewpoint pay-as-you-go plans seemed to be most desirable because of the inflationary trends in the present-day economy. In a funded plan four dollars invested today may be worth only two dollars ten years from today. The danger of a pay-as-you-go plan, however, he added, lies in the fact that the continuance of benefit payments is dependant on the continuing profitability of the enterprise. This fact makes the pay-as-you-go method more desirable, an employer commented, because the worker comes to realize his welfare is closely tied in with the continuing good health of the company. A contrasting opinion was expressed by a labor representative who considered a pay-as-you-go plan based on the continuing profitability of a company as similar to a profit-sharing plan and hence an undesirable type of pension plan.

The chairman noted that one argument in favor of pay-as-you-go plans was that at the outset the added cost of the pensions does not necessarily have an immediate effect upon production costs and prices.

Someone asked how pension payments for retired employees were met under a pay-as-you-go system when a company went out of business. Another participant explained that this problem could be handled adequately by means of terminal funding whereby, at the time of a worker's retirement, a company put away sufficient funds to continue his payments for an indeterminate period into the future.

Stabilization efforts and pension costs

The group turned its attention to the relationship between pensions and stabilization efforts under a defense economy. No consensus was reached on this general question. However, it was noted it is not possible accurately to estimate costs of pension plans, particularly the pay-as-you-type. Some participants thought these costs could have inflationary tendencies which might lead to complete government control of pension plans. Others felt, however, that such control would be highly ineffectual.

A professor contended that the government already contributes to private industrial plans by allowing companies tax exemptions on the money put into trust funds or paid out in benefits. On the other hand, the government does not contribute directly to OASI, inasmuch as this program is financed by equal contributions from employer and employee. As government purchases in a defense economy increase, he added, the government will provide a larger indirect "subsidy" to private industrial plans both because of the "tax loophole" and because it will have to pay for its purchases an estimated additional 6% to defray the costs of previously established pension plans. This transference of cost, he concluded, is facilitated by the fact that the government is not as concerned with prices as the consumer would be in a more competitive situation.

A unionist observed that the government is currently trying to plug up the tax loophole by sponsoring a law which would make employer contributions to a pension trust fund taxable. An employer said that ultimately consumers will pay for the costs of pensions because either 1) prices may go up to defray the added costs or 2) the government will raise the tax rate or lower the taxable base to make up the revenue ostensibly lost through pension fund tax exemptions. A professor suggested that government "subsidization" of private pension plans will increase as it purchases more goods for defense purposes or as the companies with such plans decide upon a more rapid amortization of past service credits.

Actuarial soundness

The chairman proposed that the group consider the basic ingredients of actuarial soundness. This brought forth a query as to the exact meaning of the term "actuarially sound." In reply the chairman suggested that a plan is actuarially sound "when the contributions one expects to make in the future have a discounted value at the present time which is equal to the discounted value of the expected future benefit payments."

A practical approach toward guaranteeing a plan's soundness, the chairman continued, might require periodic reviews of the entire program so as to reveal the possible need for some changes in the basic assumptions made when projecting the plan into the future.

Even after adjustments have been made it is still not possible to be certain, in terms of future contingencies, that a plan is sound; and this observation, he said, applies equally to self-insured and insured plans. Costs will readily vary from the original assumptions and continue to vary during the entire life of a pension program.

Objection was raised to the chairman's definition of actuarial soundness by a consultant who suggested that pay-as-you-go plans under such a definition would be considered sound as long as contributions and benefit payments are balanced.

One participant raised a series of questions. Is the main objective to make sure that a plan is economically sound or is it to set up a program which will conform with certain assumptions over a period of time? What allowances are made in the planning for shifts in the price level or for cyclical fluctuations? Is any attention paid to possible changes in the consumption pattern? Are there some criteria, over and above the usual mathematical calculations and assumptions, which could be applied to these and other similar problems?

Function of an actuary

An actuary is not in a position to consider all of these things, a consultant explained. An actuary can work out a plan with an employer or with unions and management only in terms of the expressed objectives of the company or the group involved. He does not try to tell them what they should do.

Another consultant said he felt the function of an actuary had been generally misunderstood. An actuary does not attempt to consider all the possible factors which might affect a pension plan. Rather, he first reviews what appear to him to be the most realistic assumptions with respect to mortality, interest yield, and the like; then he applies the rules of probability to these factors, and finally comes up with an estimate of cost. He emphasized that this is an estimate, and not the actual cost, which are two different things. At the end of a given period of experience under the plan, cost figures are compared with the original estimates, and if there is between the two a significant disparity which is likely to persist, then the original assumptions are changed to bring them more in line with actual experience. Someone suggested that an actuary could be thought of as a sort of "mathematical doctor."

To another participant's question as to what will make a plan "actuarially sound," the consultant replied that he did not consider the phrase to be very meaningful and therefore does not usually employ it. He cited the following definition of this term as given in a Glossary of Pension Terms published by the National Foremens Institute: "Actuarially Sound. Insurance term. As applied to pension plans, describes plan that is financially sound. Assures worker that he will receive benefits listed under plan and that payments for benefits listed will not be increased for either employer or employee." Whatever the term may mean, he concluded, this definition is entirely unsatisfactory.

Another consultant said that for himself "actuarially sound" refers to two types of situations: 1) where all the significant factors are known by the sponsor of the plan and taken into account in setting up the program; and 2) where the sponsor of a program is able to pay all of the commitments that have been made or that will be made in the light of actual experience. This brought forth a participant's comment that actuarial soundness appeared to be somewhat "ephemeral" in nature.

The consultant who had spoken earlier suggested that, although he was not prepared to describe an actuarially <u>sound</u> plan, he felt that a plan was definitely <u>unsound</u> if contributions were in no way tied to benefits as in the United Mine Workers' plan.

<u>Differences among actuaries</u>

A union man cited the case of a company which had presented to five different government agencies five different sets of figures on the cost of a pension program which was allegedly actuarially sound. These differences, the consultant suggested, arose from differences in assumptions, although in terms of <u>actual cost</u> there could be no differences. He conceded that certain differences in initial cost may depend upon the methods used in fianancing the plan, as well as upon the assumptions made. A great deal of the difference in the estimates made by union and by company actuaries in the steel industry could be traced to different assumptions, he said, particularly in connection with past service. Although past service can be funded either at a level annual rate or at an accelerating or declining rate, which mades for differences in cost at different times, nevertheless the actual total cost must necessarily be the same.

A professor agreed that in the steel case the basic difference in the estimates of the union actuaries and the company actuaries was over the question of past-service liability. He suggested that perhaps no two actuaries would ever agree on everything. This comment brought a consultant's rejoinder that if actuaries made the same initial assumptions they would probably come up with the same answers, but that there is no real need for actuaries either to make the same assumptions or to come up with the same answers. What is probably more important, he asserted, is the current profitability of an enterprise and the expectation that it will continue in business. A pension plan may not work out in a unprofitable firm which has poor prospects of remaining in business. For this reason, he said, he always encouraged as early as possible a funding of the past service liability in order to obtain the best possible assurance of payment of obligations incurred. A professor noted that in his opinion a plan was not sound unless past service credits were funded within ten years.

A government man asked how it would be possible to determine "actuarial soundness" in a situation where different actuaries using differing assumptions arrive at different estimates. A consultant referred to his earlier statement that differences in methods of financing were as important as differences in assumptions in explaining variations in cost estimates.

One participant said he had seen cost estimates from two different actuaries, one of which was almost twice as high as the other. Once the actuaries agreed on economic assumptions, however, their estimates were the same.

What makes a plan "sound"?

The only pension program capable of being actuarially sound, one consultant declared, is a government program, because of its taxing power. This brought a query as to why the United Mine Workers plan could not also be considered sound since it was based on the power of collective bargaining. The consultant replied that this plan probably was in effect sound to the extent that the union's bargaining power could keep money flowing into the fund.

The group continued to discuss the question of the actuarial soundness of pay-as-you-go plans, an issue over which there remained a considerable divergency of views.

A consultant noted much confusion has resulted from a misconception that U. S. Treasury approval of a plan necessarily guarantees its actuarial soundness.

One consultant emphasized the close relationship between actuarial soundness of a plan and financial soundness of the firm. He noted that before pensions became a collective bargaining issue the general attitude of employers was to make every effort to pay off past service as quickly as possible, but that now many companies are holding back "to see which way the wind blows" before making any large commitment in the way of funding past-service credit. A professor responded that he was under the impression employers were trying to fund past services as quickly as possible. The consultant agreed that while this was true in some cases he knew of many others who were not doing this. He conceded, however, he was not sure what the trend was.

A union man commented that he knew of many companies desiring to pay off their past service liability as quickly as possible, frequently because of the tax-credit inducement. Another unionist suggested that in a competitive situation a firm which funds its past-service liability rapidly puts itself in a more favorable position than a company which holds back. The first unionist, however, added that as long as money to pay benefits was available it did not make any real difference whether it was in a fund or in current surplus or reserve.

A consultant replied to this last remark that, although in the final analysis there probably was little difference, from an accountant's point of view considerable difference would result from charging pension costs against one period or against another. The chairman added that paying off past service too rapidly might also have some effect on production costs when the larger contributors to fund past service are charged to current production.

Maintaining soundness

A consultant wondered whether experience with pension plans over the last decade could suggest a proper course of action. He pointed out that this period has been one of high profits and high wages, and that plans which had been viewed as actuarially sound during the thirties have been condemned as unsound during this past decade because the benefits turned out to be inadequate. He asked whether there was any formula for determining what changes may have to be made in the future to maintain soundness.

Another consultant explained that in order to maintain pension plans on a sound basis revision was usually an annual, rather than 10 or 20 year, proposition. In reply to a question, he admitted this implied that a pension program involves an "open-end commitment," at least in a legal and moral sense, although he noted that there could be bona-fide grounds for discontinuing a pension plan.

A professor said he felt it reasonable to consider a plan as sound if the actuaries involved had based their proposals on the best possible assumptions at the time. Actuaries should not be held accountable for such things as changes in the price level and other circumstances beyond their control or beyond their ability to foresee.

A government man ventured a prediction that for the near future at least current pension plans will find themselves in a very favorable position on the basis of their early assumptions. He pointed out that a war-geared economy would continue for some few years, while actuaries had based their assumption largely on data relevant to a period of a lower employment and earnings level than is likely to prevail from now on.

A consultant suggested that the objective should be financial soundness rather than mere actuarial soundness. In his experience he had found that employers frequently tend to underestimate the cost of a pension program so that as the plan expands their problems become more acute. He asked whether it is not somebody's responsibility to play up the cost factors to the employer rather than to minimize them.

In reply, the chairman observed that part of the problem stems from the fact that employers often start out to pay for a plan which they think will be adequate and are not sufficiently aware of how much more it will cost to make certain improvements which they come to feel are desirable.

The cost problem, a consultant asserted, has both an economic and an actuarial aspect, and actuaries could be counted on to provide more accurate estimates of actual costs if economists could furnish them with some reliable economic assumptions. In the absence of this aid from the economist, the actuary must still base his valuations upon a certain set of limited assumptions relating to mortality, interest, and the like.

Following some additional discussion on the subject of the cost of a sound plan, a participant raised the concrete question as to how an actuary would procede in estimating the age of actual retirement. The chairman replied that on this point an actuary might use any of the following: 1) the experience of some other plan, 2) age 65 with certain allowances or 3) his own judgment in the matter. An additional alternative was suggested by a consultant to the effect that an employer could make the decision after the actuary had discussed with him the various possible assumptions and their respective implications as to cost.

The objection was raised that on many points employers were not in a position to make an intelligent decision on their own responsibility. To this a consultant replied that he felt actuaries had performed their duties when they had explained to the employer what might reasonably be expected to result from a given decision. The chairman added that in fact actuaries usually try to warn an employer whenever he might appear to be assuming too heavy an obligation.

Citing the experience of the Social Security Administration, where one set of estimates is barely completed before a re-appraisal of the situation in the light of changing circumstances is begun, a government man pointed out that both public and private plans need constant revision, constant re-appraisal, and new estimates. It is important for the people responsible for both types of plans to be aware of the fact that they are faced with constant changes. Fortunately, he added, the last few years have seen increasing wages and employment, a factor which has made it possible for most pension plans to be on the safe side on their dollar commitments.

5.

Special Problems in Collective Bargaining on Pensions and in Administering Pension Programs

Chairman: Charles W. Anrod, Loyola University

Policy on veterans

The chairman raised the problem of dealing with employees under private industrial pension plans who are currently being called into the armed services. Under a plan with which he was familiar the decision had been made to give full credit to employees who had been in service during World War II. However, there was an uncertainty about what to do in the present situation because there was no accurate way of judging how many men will go into service and how much it would cost to keep up their pension credits.

An employer reported that his company had not yet adopted a policy on the matter, although he anticipated employees in service would be given a "leave of absence" and receive credit for their period in service. However, he admitted that there was a good deal of uncertainty over what would be the best policy.

When sufficient data become available and the extent of the problem is known, a consultant observed, employers will be in a better position to work out a policy.

Pointing out the relevance of an interpretation of the Selective Service Act in dealing with this problem, a government man suggested that the courts may rule that men going into service must be given full credit in both contributory and non-contributory plans. Although the chairman did not believe the present law would permit such an interpretation, the government man was inclined to feel it was impossible to predict the court's action and also noted that Congress might revise the law along these lines.

The chairman stated he did not expect that companies would be forced to pay for assumed credits accumulated by an employee in service, but that the period of service would not be viewed as a break in continuity of employment.

The government man added that if a pension were viewed as deferred wages credits could be given the employee in service as if he were still employed by the firm. Agreeing that military service probably would be considered a "leave of absence" in both contributory and non-contributory plans, an employer suggested that management might give a returning serviceman an opportunity to make up his payments. He admitted, however, this would impose a considerable financial burden on the individual employee. Another government man noted that under a pension plan with which he was acquainted benefits equal 1% of the average earnings over the last 10 years multiplied by the number of years in the employ of the firm. Under a commitment such as this, he suggested, the firm may have to pay for the years the employee spends in service.

One participant wondered whether the relatives of a man in service would be eligible for benefits if the man was killed while in the service. The chairman replied that in such an event, under a conventional contributory pension plan, the beneficiary would receive the man's contributions plus interest. A unionist explained that under the plan sponsored by his union a worker continues to be covered while in service under the retirement and also the family hospitalization and surgical benefit provisions -- an arrangement which helps reassure the serviceman that his family will be provided for while he is away.

Optional retirement age

The chairman moved the discussion to the topic of "normal and optional retirement dates." For a short period the group again gave its attention to the normal retirement age of 65. The arbitrary character of this particular age and the difficulties involved in making it compulsory were again noted. Attention then shifted to the use of early retirement provisions in pension plans.

The chairman explained that under such provisions benefits usually decrease sharply for every year a man retires before the normal retirement age -- roughly calculated at a drop of 5% in benefits for each year. He wondered whether union members ever made use of the early retirement dates. A union representative replied that although workers may never exercise their right of optional retirement at an earlier age (such as 55) they still like to have such a provision in the plan. He said this was particularly true of younger workers, who often thought of 65 as too advanced an age to wait for retirement.

A university professor warned against confusing an optional early retirement age with a provision for retirement in the event of total and permanent disability. An early retirement age was undoubtedly more important to some people -- for example, professional workers -- than to others. The chairman said his experience also indicated that an early retirement option was probably more important to professional workers than industrial workers.

Attention was then drawn to another category of retirement options -- that in which the optional age, being higher than the "normal" retirement age, constitutes an alternative to compulsory retirement at a specified age. It was noted many plans provide that if a man who had chosen an optional form of retirement allowance keeps on working past the specified retirement age and dies on the job his survivors receive no benefits. This brought forth the comment from an employer that such a provision was causing his company to lose the services of many good men before their usefulness to the company had begun to decline. To overcome this problem, he related, his company occasionally resorted to the subterfuge of "retiring" these men at the normal retirement age, in order to protect their survivors' benefits, and then "rehiring" them.

Optional forms of retirement allowance

Problems in this field are often created by a lack of understanding of the various options, a consultant observed. He explained that in plans he prepared he put a special effort into making the alternatives very clear to covered employees so that they could make the choices which suited them best. Usually, if a worker wanted to keep on working past the normal retirement age he could have the following two options: 1) to become eligible for larger retirement benefits whenever he did retire with the understanding that his survivors would not be eligible to any benefits if he died while still working; or 2) to accept a lower scale of benefits with the understanding that they would be paid to his survivors if he died while still working. The chairman added that he is acquainted with still another option whereby a worker chooses to accept a smaller benefit, with the understanding that one-half of the benefit will be paid to his survivors if he dies.

A consultant pointed out that in his opinion giving options does not increase the cost of a plan.

A government man asked whether anyone had information as to which options workers seemed to prefer. A consultant replied that today two out of three choose the survivors' option in those plans where it is offered, although 10 years ago one out of three chose the survivors' option.

Another consultant reported that at one plant in the Middle West 90% of all workers had selected the survivors' option, but largely because the company had vigorously advised the workers to take this option. In other plants he was acquainted with, only a small percentage of the workers took this option. A plan does not sell itself, he concluded, and its acceptance usually depends upon the policies and recommendations of interested parties. The chairman agreed this was true, and added that he thought the survivors' option plan provided a protection more workers would select if they were adequately informed about the plan. An employer said that many workers at his plant had selected a contributory over a non-contributory plan largely because the former offered joint options.

Despite the fact that in his opinion a joint option feature did not cost more, a consultant stated, unions have failed to push for its inclusion in non-contributory plans principally, he felt, because the current practice is to tie benefits in with social security.

A participant asserted that in his opinion unions were unwise to tie their plans in with social security and that they should push more vigorously for joint option features. A unionist noted that some plants under contract with his union do have joint options in their plans, but explained that his union, generally, tended to avoid such plans because they were usually on a contributory basis. Unions have just entered into the pension area, he added, and undoubtedly will become more interested in the "refinements" as they become better acquainted with the whole subject.

Contributory vs. non-contributory financing

"The merits of the contributory vs. non-contributory issue" was the next topic which the chairman asked the group to consider. A consultant led off the discussion by asserting that a complete "second layer" in the pension cake can only be obtained on a contributory basis. If union workers appreciated the fact that their present plans were limited because of cost considerations they would tend to support contributory plans in place of the non-contributory plans they now have.

One union man agreed. He told of his experience with a union group to whom the alternatives had been carefully explained and who voted solidly in favor of a contributory plan since it gave them more substantial benefits.

Another union man took exception. He said that under the existing tax laws non-contributory arrangements can purchase more insurance than can the joint funds to which employees contribute. He explained this was because the workers' money is taxed before it reaches the fund whereas under non-contributory plans the employers' contributions are not taxed. A third unionist cited a recent article in the New York Times indicating there had been a shift from contributory to non-contributory plans largely because of the tax exemptions involved.

The unionist who had spoken first restated his position by saying unions had made a mistake in tying their pension plans to social security and the one way to undo that mistake was to make their plans contributory. Another unionist contended it could be demonstrated that a worker can get a larger annuity by investing his money in United States government bonds than through a contributory pension plan. To this a consultant replied that the taxes on the income from government bonds would cut down the size of such "annuities."

Another consultant reminded the group of the fact of the defense economy and of the importance of meeting the cost of this defense program. He hoped that money would not be diverted from defense purposes, but he felt this was happening under non-contributory plans when companies transferred the cost of pensions to the government in the form of higher prices for defense goods. This increase in cost, he asserted, would have a general impact upon the price structure, because an increase in costs exerted a greater inflationary pressure than quantity of money in circulation. Pensions add to the cost of goods and therefore generate greater inflationary pressures.

A union representative felt that such an argument was not decisive because in both contributory and non-contributory plans the final cost would be about the same, inasmuch as unions would tend to demand higher wages to make up for the workers' share in contributory plans.

One consultant gave it as his opinion that a contributory plan offered the worker more assurance his plan would still be in existence when he retired, and probably would be more "financially sound" than a non-contributory plan. However, he suggested that it might be possible to have a non-contributory "base" up to $3,600 a year and then make the plan contributory from there on. Under this arrangement the employer would pay for all credits on the first $3,600 the worker earned each year, and from that point on for the remainder of the year the plan would be contributory. He urged unions and management to seek a "middle ground" and conceded the point that non-contributory plans also had certain advantages.

The chairman expressed the view that contributory plans best fit into the philosophy of collective bargaining and the analogy of the "three layer cake." He found it somewhat difficult to understand how unions could reasonably demand joint administration of pension funds if their members failed to contribute to them. Contributory plans conform to the conception of a "partnership" between union and management created through the collective bargaining experience. He felt that union objections to contributory plans could be overcome if the government permitted employees to claim tax exemptions for contributions to pension plans as is the case in Great Britain and Canada, although he noted he did not know of any union which actively supported such a tax provision. He said although he was not sure that he agreed with the opinion of another participant that non-contributory plans had a greater inflationary effect than contributory plans, on the economy, he thought unions ought not to support anything which encouraged inflation. He noted the group had been in quite general agreement that inflation was the "number one enemy" of pension plans.

A unionist responded that he could not understand how contributory pension plans were any less inflationary than non-contributory plans since the cost was the same.

The chairman asserted that contributory plans would make a union more "responsible" and give workers the feeling that it was "their plan," a feeling they did not have under a non-contributory plan. The unionist said he had not observed that there was any difference in the workers' "feelings" about the plan in the two cases, and remarked that an employee can just as readily figure out how many service credits he has accumulated under a non-contributory plan as he can if he is covered by a contributory plan.

The chairman declared that a basic tenet of free enterprise capitalism was for people to provide for themselves as much as possible, and, therefore, that it was desirable for every worker to put a few dollars out of his pay each month into a pension fund to provide for his own future. In summary, he noted that there appeared to be no general agreement on the "contributory vs. non-contributory" issue, and suggested that the group move into a discussion of "joint administration."

Joint union-management administration

A unionist opened the discussion with the explanation that his organization was interested in joint administration solely as a means of making sure that the plan was conducted honestly and in conformity to the stated objectives of the plan. He pointed out workers are entitled to know how the plan is administered because in many cases they have sacrificed a wage increase for the pension program. Joint administration can help avoid misunderstanding and suspicion. Another unionist supported this point of view, citing instances in his own experience where workers had developed completely unwarranted fears of employer dishonesty in operating an employer-administered plan. He concluded that joint administration could eliminate mistrust and give workers the feeling that they are working together in a "team" with management.

The chairman explained that he favored joint administration for the same reason that he favored a contributory type of plan, because both features help management and workers to get closer together as a working team in solving the problems of the program. With worker representation on administration, chances for misuse of funds are reduced. He said he sympathized with certain complaints voiced by union representatives over bad handling of funds in the past. In addition, he said, joint administration can be of great value in developing union leadership as well as in building general union responsibility.

Experience with several programs, a consultant said, has convinced him that unions are usually not much concerned over the investment aspect of administration. Their primary concern is to see that full benefits are paid according to schedule.

The chairman agreed that his experience in the field also confirmed the observation that unions, generally speaking, were not interested in the investment of funds. On the other hand, they showed a great deal of interest in what he called the "net premium." He referred to the so-called "dividends" which are paid back by the insurance company to the employers under some insured plans, and declared that they often tend to hide the true cost of a pension program. Frequently, he said, a union might never be informed about refunds and therefore had no idea how the refunds, if prorated over the entire work force, would reduce the premium per individual.

The consultant said this was part of the general problem of deciding how best to redistribute the refunds made by insurance companies when premiums proved to be in excess of the amount necessary to keep the plans in operation. Since it would be difficult to try to credit any amount to the individual's account, he said, one way to deal with this problem would be to put the entire refund back into the fund so that it can be used only for the employees' benefit through improvement of the program.

Referring to the whole discussion of joint administration, a professor observed that although there had been no expressed opposition among the group to the desirability of joint administration, it was unwise to assume that there was a general concensus on the matter. He noted that in many cases the issue of joint administration is closely related to matters which are often considered to be "management's prerogatives," and that this group had not had the opportunity of exploring many of the complexities of the issue.

Trust agreements and investments

On the subject of investments of funds under self-insured plans the chairman noted that the trust agreement frequently placed certain restrictions on the freedom of the trustee to invest the funds. In the discussion, a case was cited where the trustee was not permitted to invest the funds in a union bank. In other cases a high percentage of reserve was required to be in government bonds. A consultant added that, on the other hand, he knew of several situations where both union and management had wanted the trustee to be given complete freedom in the matter of investing funds and desired merely to be advised of all action taken.

One consultant said that his firm favors giving the trustee freedom to invest funds as he sees fit -- even in common and preferred stocks when it appears to be advisable. Personally he would put a large portion of funds into stocks. This could in some measure be helpful in conteracting inflation, he said. In addition, funds invested in stocks can gain a competitive advantage over insurance funds because they would be able to earn 3 1/2% or more on stocks as against the 2 1/2% earned by many insurance companies. A higher yield can become very important, he noted, and one-half percent increase in yield can provide as much as 15% additional benefits over the period of a generation.

The chairman was inclined to feel, on the other hand, that through investment in stocks the fund ran the risk of having to be completely liquidated. The consultant replied that he believed the risks tended to average out in the long run if the trustees would decide to "stay in the market." In answer to the objection of another consultant that a depression could create a very serious problem for such funds, he said that the important thing was for the trustees "not to lose their nerve" or try to pull out of the market. Even in a serious depression the risks would not be too great. He said he had calculated that, assuming a 10-year long depression with 50% of a pension fund invested in common stock, the fund would actually experience a net depreciation of only about 16%. He admitted that this might be hard to believe but asserted that he could prove it mathematically.

Liquidation provisions

Under the final topic of "liquidation provisions" the chairman asked the participants what measures they felt should be taken in the event of liquidation of a pension program. A consultant reported that his firm invariably advised against any immediate liquidation of the funds, which should be protected so as to continue to provide benefits for the employees covered. In addition, he favored some provision for putting sufficient funds into escrow to care for those already on retirement. If anything were then left over, he said, it could be prorated to the rest of the employees on some equitable basis.

Another consultant observed that a plan with provision for "terminal funding" would have no problem in the event of liquidation and agreed that a prorating of all excess funds among employees close to retirement would be a satisfactory solution. Another participant added that such a step was presumably based on the assumption that younger workers would have a better chance than the older workers of "starting over" on a retirement program.

A member of the group asked whether there were usually any differences in the liquidation provisions of contributory and non-contributory plans. The chairman replied it is assumed that in contributory plans the employee's contribution would always be returned and that only what was left over would be liquidated.

The formal discussion of the conference closed at this point.

Note: These proceedings were prepared by John M. Brumm based on notes taken by Louis Boffo and Arnold Weber, all on the staff of the Institute of Labor and Industrial Relations, University of Illinois.

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