BULLETIN 21
JULY 1952

PENSION PLAN POLICIES and PRACTICES

Michael Puchek

NEW YORK STATE SCHOOL OF INDUSTRIAL
AND LABOR RELATIONS, CORNELL UNIVERSITY

A publication of the
New York State School of Industrial and Labor Relations,
a unit of the State University of New York,
at Cornell University

Single copies of this bulletin will be sent upon request free of charge to residents of New York State. In the case of bulk orders (more than five copies) and out-of-state orders, a nominal charge will be made to cover direct costs (25¢ per copy in the case of this bulletin).

Pensión Plan Policies and Practices

Recent Experience of Eleven Pension Plans

Michael Puchek

Bulletin No. 21 July 1952

New York State School of Industrial and Labor Relations
Cornell University Ithaca, New York

ABOUT THE AUTHOR

MICHAEL PUCHEK took his B.S. degree in business administration at Boston University in 1948. He received the Master's degree from Cornell in 1950. After graduation, Mr. Puchek joined the staff of the New York State School of Industrial and Labor Relations as research associate and continued in that position for a period of two years.

Presently, he is employed by the Board of Administrative Policy, Wage and Hour and Public Contracts Divisions, U. S. Department of Labor, Washington, D. C.

ACKNOWLEDGMENTS

THE WRITER is particularly indebted to Professor John McConnell, of the New York State School of Industrial and Labor Relations, who not only conceived the idea for this study but also offered many helpful suggestions during its development. Thanks also go to Professors Robert Aronson and Duncan MacIntyre for their generous assistance during the preparation of this bulletin.

CONTENTS

LIST OF TABLES

Introduction

Industrial pensions are rapidly achieving a previously unknown importance for all groups in the community. With the spread of pensions over substantial areas of industry and trade, especially since World War II, more employers and employees than ever before must grapple with the technical problems involved in the financing and administration of such benefits. Consumers, too, have a practical interest in the effects of pension plans on the cost of goods and services and, indirectly, in the incidence of such plans on the distribution of the tax burden.

Scope and Objectives

The main purpose of this study is to analyze the design of certain industrial pensions, the purposes they are supposed to achieve, and the administrative and financial problems which arise in their operation. It attempts to describe and analyze the procedures used and the policies developed in the construction of a plan. It also analyzes the provisions of eleven plans and, where available, the operating experience in order to determine how well these plans achieve their objectives.

This study is a record of pension experience. It was undertaken with the purpose of providing to those interested in pension planning the story of pensions among small and medium-sized business enterprises in a single geographic area. Generalizations about pensions as a whole would be unwarranted on the basis of the facts reported, but the insights into the thinking of employees about their plans and their experience with them may be enlightening.

Coverage of the Study

The eleven firms studied here are located in Western New York State. A list of the pension plans adopted by these companies is contained in Appendix A, page 53.

The eleven plans do not in any sense constitute a sampling of private pension plans. An intensive study of a few plans, primarily among small and medium-sized employers, was considered a more desirable approach than a survey of more general aspects of a larger number of plans. There is no special significance to be attached to the eleven plans.

Data concerning these plans were obtained during the late Spring and early Summer of 1950. Six of these companies employ less than two hundred employees. Three employ two hundred or more employees but less than one thousand persons, while two other companies employ more than four thousand employees. The companies include both manufacturing and nonmanufacturing concerns. Seven are primarily metal fabricators. Four other firms are service establishments and handle such items as industrial supplies and equipment, steel, millwork, and farm equipment and supplies.

Nine of the plans were employer-initiated. Two other plans were adopted through the process of collective bargaining. Despite the legality of such bargaining, at the time of this study, no employer-initiated plan had been brought within the scope of collective bargaining.

Method of the Study

Except in one of the eleven cases studied, data for this study were obtained from interviews with personnel who had an official relationship with the design and administration of the pension plans, and from documentary sources supplied in each case by such personnel. In one case, however, an opportunity was afforded to observe negotiations between company and union representatives leading to the establishment of a pension plan.[1]

Origin of Plans

Most pension plans were adopted, during the past decade, under the influence of four economic and legal factors. They were (1) the structure and incidence of federal taxation, particularly excess profits taxation, (2) wage and salary stabilization policies during World War II, (3) labor shortages, and (4) the National Labor Relations Board's ruling that pensions are legally bargainable.

In each of the eleven plans studied here, however, these factors varied in importance. Among all of the plans the incidence of taxation was undoubtedly important. In a majority of the cases, wage stabilization policies and acute labor shortages were influential. The ruling of the NLRB, favorable to pension bargaining on the other hand, was less influential, since a majority of these plans were adopted before 1948.

Despite their varying importance, at least one of these factors affected the adoption of a pension plan in every case. The following comments by management officials are illustrative:

[1]Comparable operating experience was available for only a few plans. Cost experience for only two plans, and partial cost experience for one other plan was also obtained. Detailed breakdowns of the composition of current pension plan membership were available in four cases only. A complete record of membership experience was obtained from only five plans. Although statements concerning general labor turnover rates were obtained from a few company officials, quantitative data supporting the statements were not available.

> One of the methods of granting employees something 'extra' was to adopt a pension plan for their benefit. . . . The plan cost very little to install because an excess profits tax of 85 percent was in effect.
>
> The pension plan was established during high profit years. At that time high corporate taxes were in effect, including an excess profit tax. This factor led the (then) owners, after discussion with advisors, to institute a plan.

In addition to general forces, local labor market conditions facing individual employers also prompted the adoption of pension plans. Employers often expected that pensions would reduce labor turnover and attract new employees. Among the companies studied here, for example, one employer remarked, "The pension plan is one way of getting people to stay with you." Thus, with a more stable work force, efficiency would be enhanced. The plan, moreover, especially in future years, would provide a satisfactory vehicle for the retirement of superannuated employees.

A sense of social obligation and the promotion of good will may also be influential in the adoption of a pension program. By the provision of retirement income for individual employees, many employers expect to discharge a social responsibility and, at the same time, to improve their public relations. The comments of a steel mill executive are typical. "After an employee has been around for 25 years or more," he remarked, "he is entitled to some kind of pension from the company."

The following six chapters discuss the problems encountered in adopting plans, the policies finally adopted, the problems in effectuating these policies, and the impact of these policies on various groups of employees. For the convenience of the reader, a glossary of technical terms is given in Appendix D.

CHAPTER I

FUNDING METHODS AND EXPERIENCE

Few companies are in a position to purchase pension benefits through a lump-sum payment. Since large financial outlays are involved, employers normally fund their plans through payment of relatively small amounts which, nevertheless, will be adequate to provide benefits.

Nine of the eleven plans studied here provide for benefits through one of four common methods of funding.[1]

Methods of Funding

The four methods of funding[2] used by the nine plans include (1) level premium accumulation, (2) level percentage of payroll, (3) single-premium deferred life annuity, and (4) level percentage of profits of the company. The method of funding is generally associated with a particular type of plan.

1. The level premium accumulation method is normally used with insured individual annuity pension plans. This method involves two considerations: first, the determination of the amount of cash required at a selected retirement age to produce a given income and, second, the establishment of a level annual payment, prorated from date of joining to retirement date. Expected interest is the only actuarial factor used in calculating the premium. Expected mortality and withdrawals are not considered since these plans are usually vested and normally pay a death benefit.

2. Uninsured self-administered pension plans commonly use the level percentage of payroll method of funding. This method anticipates all major events which may be expected to occur in the operation of a pension fund. Mortality, interest earnings, and withdrawals from employment prior to normal retirement, and anticipated salary increases, among other actuarial factors, are accounted for in arriving at an estimated annual pension contribution, stated as the level percentage of payroll.

3. The single-premium deferred life annuity method is customarily used with insured group annuity plans. This method involves the purchase of a series of units of paid-up deferred annuities, one unit to be

[1]In the case of the two union-negotiated plans, funding methods had not been selected at the time of the study.

[2]Hugh O'Neill, *Modern Pension Plans* (Principles and Practices), New York: Prentice-Hall, Inc., 1947. Pages 81–89 contain a detailed discussion of methods of funding.

purchased each year for each eligible employee to cover accrued retirement benefits. In the calculation of the premium amount, consideration is given only to expected interest earnings and to anticipated mortality before and after retirement age. This method does not discount for withdrawals.

4. The level percentage of profits method is commonly used with uninsured profit-sharing retirement plans. Pension contributions are a fixed percentage of net profits. No specific annual amounts are required. Because profits fluctuate, the employer's contribution varies from year to year. In years of no profits, contributions cease altogether. No actuarial factors are involved in this method.

Factors Influencing the Selection of Funding Method

Of the nine firms studied, six are individual annuity plans, one is a self-administered trusteed plan, one is a group annuity plan, and one a profit-sharing retirement plan.

Individual annuity plans. Three factors probably influenced employers of the six firms that adopted individual annuity plans: (1) size of the organization, (2) employers' desire for certain additional types of benefits, and (3) inherent advantages in the funding method, particularly at the time of adoption.

1. Certain aspects of the size of the group to be covered made the selection of individual annuities the only practicable method of funding. Group annuities were not available for three of the firms (Companies C, E, and H) because a minimum requirement of fifty participating employees could not be satisfied.[3] The size of the initial participating group, in those three cases, was 35: 8 and 27 employees, respectively. In three other cases (Companies A, B, and D), each with 50 but less than 100 participating employees, wide fluctuations in employment made group annuities impractical. (Underwriting rules usually give the carrier the right to refuse to accept further premium payments if the participating group falls below 50.[4]) Moreover, group annuity contracts have certain other undesirable features, particularly for the small employer; first, a certain minimum annual premium income is required, customarily $10,000 annually[5] (in one case studied here, Company E, the first year's gross premium was less than $4,000); second, major insurance companies limit the amount of annuity income that may become payable to any eligible employee.[6] Thus, the relationship

[3]*Ibid.*, p. 128.
[4]*Ibid.*, p. 129.
[5]*Ibid.*, p. 128.
[6]*Ibid.*, p. 130.

of benefits to wages, in the case of the higher paid employee, could not be maintained.

Self-administered plans, on the other hand, are usually impractical for small organizations because of the special skills and additional work that may be required to handle them. Company A's president, for example, stated that he did not want to go into the insurance, banking, and investment business. Moreover, all six individual annuity plans were established in a period (November 1941–July 1943) when the labor supply was short,[7] and employers were exerting all efforts to increase war production.

Finally, the funds available from small organizations are usually insufficient both to maximize earnings and to provide fund security through investment diversification. For example, Company E's annual premium did not exceed $5,000 in 1949. Even in a somewhat larger plan, Company A, the 1949 premium did not exceed $13,000.

2. The desire to provide certain types of additional benefits, such as death or disability benefits or dismissal wages, influenced several employers to adopt individual annuity plans.[8] For example, Company A's president remarked, "One of the main considerations for adopting the individual annuity type of plan was that employees have to their credit certain cash values. In case the employee withdraws, or the plan is terminated, he cannot receive less than the present cash value of his contract." In addition to retirement benefits, all six individual annuity plans studied here make certain provision for disability benefits and vesting (dismissal wage), and, in five cases, for death benefits.

3. Because of the high initial outlays involved in level premium accumulation, the individual annuity plan offers two other advantages to employers. One advantage lies in the possibility that future premium costs will be reduced as withdrawals occur. Several companies studied here have experienced considerable postwar labor turnover — male employees changing jobs and female employees leaving the labor force. Many of the withdrawing employees, although plan members, failed to qualify for vested rights. Thus, employer contributions made on their behalf were retained in the plan and used to reduce current premium outlays. At Company D, for example, during the period 1945–1947 less than one third of a group of 49 withdrawing plan members received any benefits. The second advantage is that high initial premiums result in proportionately greater tax offsets, particularly when

[7]Leonard P. Adams, *Wartime Manpower Mobilization*, Ithaca, New York: New York State School of Industrial and Labor Relations, Cornell University, 1951, p. 1.

[8]Because this funding method involves the creation of individual cash sums, more than any other method it lends itself to a wider variety of other uses, as well as retirement.

the tax structure is burdensome. The six individual annuity plans studied here were adopted during 1941–1943 when excess profit rates, as well as high corporate taxes, were in effect.

Self-administered trusteed plan. Several reasons influenced the firm adopting the self-administered trusteed plan. The main reason was that the company believed it could realize, in the long run, more benefits on pension contributions. A management representative stated that they expected annually to better the interest rate "guaranteed" by insurance companies by at least ½ of 1 percent.

Moreover, certain aspects of the company's size made a self-administered plan possible. Since a large group was involved (over 1,900 participants), actuarial assumptions — such as mortality, disability, and separation (quit and discharge) rates — would be expected, more nearly, to approximate experience. Funds would be sufficient to allow diversification of investments. (Actually, within five years after plan adoption, funds in the pension trust funds were in excess of two million dollars.) Personnel skilled in investment management would be available. (Two officers of the company have extensive experience in the investment field.) Finally, because pension contributions were not allocated to individual accounts, administrative simplicity and a saving in cost would be achieved.

Group annuity plan. Security of assets, contract terms, and services performed by the insurance carrier influenced another firm to adopt a group annuity plan. There is no evidence to indicate that any other method of funding was considered. The bids of five insurance carriers were evaluated, however, before decision was reached to sign with a large mutual insurance company.

Profit-sharing retirement plan. The president of Company G stated that his company, in 1947, adopted the profit-sharing retirement plan because this method of funding assured maximum funding flexibility.[9] He said that past experience showed that his company's earnings fluctuated widely. Rather than assume the burden of a fixed annual individual annuity premium, the company decided upon a profit-sharing retirement plan requiring no contributions when there are no earnings. Since this company invests all pension contributions in government bonds, no attempt is made to maximize interest earnings of the trust. However, financial security of the plan is assured.

---

[9]In the World War II period this company considered and rejected an individual annuity plan. The president regrets that a profit-sharing retirement plan was not brought to the attention of the management at that time. Earlier adoption, he feels, would have had two advantages: employees facing retirement within five years would have had more substantial pensions, and the net cost to the company would not have been large since an excess profits tax was in effect.

In one other case studied, a profit-sharing plan was considered and rejected as a substitute for an existing individual annuity plan. According to the president of Company E, lack of fixed pension benefits, on the one hand, and the distribution formula, on the other, would lead to skepticism and distrust on the part of workers, thus weakening the incentive value of the scheme.

Selection of an Insurance Carrier

Of the seven firms that funded through a commercial carrier, only two companies studied bids from more than one insurance company before signing a contract. One of these has been discussed above. The other firm, after considering bids submitted by two companies, finally decided to purchase individual annuity policies from both companies. Thus, for a majority of the companies with insured plans, the selection of an insurance company was a minor consideration. Usually, the selection of an insurance agent meant that contracts would be purchased from the insurance company which he represented.

Two reasons explain why employers did not attach particular importance to the selection of a commercial carrier. First, there was a belief among some employers that the contracts of the several insurance companies are similar. For example, Company H's treasurer stated, "Policies written by insurance companies have very little in the way of differences." Yet, the individual annuity policies of several large stock and mutual insurance companies vary in net premium costs and in the amounts retained in the event of withdrawal, particularly in the case of short periods of membership. Moreover, in the event of withdrawal – quit or discharge – after one year of participation, some insurance companies retain the entire first year's premium.

Second, some employers make little distinction in the purchase of annuities and other insurances, such as fire, health, and the like. They normally consult with and buy from the insurance agent with whom they have already established a working relationship.[10] For example, Company B's treasurer indicated that the insurance agent who wrote the plan (now a broker) writes other insurance coverages for the company. As indicated below, in at least five of the seven cases studied here, the first insurance agent contacted received a share of the annuity business.

[10]This method of adoption has serious limitations. In the design of the plan, employers rely to a great extent on the technical competence of the insurance agent. In some cases, although agents possess competence in the insurance field, they lack the highly technical skills required for pension plan design.

Union-Negotiated Plans

In the foregoing voluntary plans, the selection of a funding method was made in conjunction with the design of the plan. The two firms that adopted union-negotiated plans (Company F and I) did not follow this procedure. There, the entire plan, except for the method of funding, was agreed upon in collective bargaining sessions. Funding was not a bargaining issue and entirely discretionary with the managements concerned.[11]

The absence of precedent in the matter of funding (in basic steel), and the willingness of the local bargaining unions to believe that the employer was morally obligated to develop adequate pension reserves, explain why funding was not an issue.

At Company F, several months after the pension agreement was signed, the management had not agreed upon a method of paying for pensions. Two methods, terminal funding and pay-as-you-go, were, however, under consideration.

Funding Experience

Many of the firms were concerned with increasing pension costs. This was particularly marked in five of the six firms utilizing individual annuities. On the other hand, one company that employed a self-administered trusteed plan, appeared to be satisfied with its funding experience.

Individual annuity plans. The experience of Company C is illustrative of the concern with rising costs of five of the six firms with individual annuity plans. The controller of that company indicated that costs were shared almost equally by employer and employee at the time of adoption — 1941. Since 1945, however, the employer's share has risen steadily. In 1949, the employer paid 80 percent of the total premium; employee contributions accounted for the other 20 percent. The chief reason for this growing disparity between employer and employee contributions is a provision in the plan which restricts employee contributions to a maximum of 3 percent of compensation. Because of the direct relationship between final wages and benefits,[12] rising wage levels together with the increasing age of members require a proportionately larger premium. The employee contribution of 3

[11]Although funding was discussed in both negotiations, the subject was not an issue. For example, at the Company I negotiation, the union's strategy board injected the "new" issue — funding — merely as a bargaining tactic in an attempt to win small concessions in other areas of the plan. Never did the union seriously consider taking a firm stand for a "definite" funding commitment.

[12]Benefits are 40 percent of compensation and premiums are adjusted annually, until age 60. Subsequent wage changes have no effect on benefits.

percent of current wages does not increase at the same rate as the premium. Therefore, additional employer contributions are necessary.

Extensive cost experience was secured from two firms, Companies A and B. Their experiences differ widely. Company B's premium payments have risen rapidly. In 1949, premium payments exceeded those for 1946 by 49.8 percent. In contrast, Company A's premium payments, in the same period, rose less than 4 percent. Several factors explain Company A's relatively stable cost experience:

1. Postwar wage increases were not granted by this company to the same extent as by some other firms, particularly unionized firms.
2. In the later years of employment (after age 45), wage increases must be extraordinary before they can affect the benefit level.[13]
3. This firm's work force has been relatively stable during the entire past decade; the pension plan also has a stable membership group.
4. There have been few withdrawals from the plan.
5. Two-thirds of the withdrawing participants, in the period 1944–1949, were ineligible for vested rights. Contributions made on their behalf reverted to the trustee of the plan and were used to reduce current premium outlays.

Experience of both of these plans shows how age and sex differences may account for cost differences. For example, in 1949, at Company A, the average hourly cost for all participants under age 50 was 7.1 cents; however, average hourly cost for all participants over 50 was 14.1 cents, or an average difference of 7 cents per hour. Sex also makes for differances in premium outlay, mainly because of wage differences between male and female employees. At Company B, for example, in 1949, premiums for female members were at the rate of 8.2 cents per hour, whereas for male members 22.9 cents per hour were paid.[14] There, age also was a factor since the average age for females was eight years below that for males.

Both plans also show significant differences in annual premium outlay. In 1949, Company A's average annual premium cost per participant was $200.49, equal to an average cost of 10 cents per hour, based on a 2,000-hour year. On the other hand, Company B paid $395.89 per participant, or 19.8 cents per hour. More liberal benefits, on the one hand, and differences in the composition of the plan's membership, on the other, explain the absolute differences in cost.[15]

---

[13]See p. 28 (Company A), for a more detailed discussion of this point.

[14]Absence of females in executive and supervisory positions accounts in large measure for the difference. For example, eliminating executives and supervisors narrows the differential to approximately five cents.

[15]Company B was funding an average monthly benefit per participant of $58.38. At Company A, $34.50 monthly was to be provided. Company B provided full vesting; at Company A two years

Self-administered trusteed plan. Financial experience of the self-administered trusteed plan of Company K appears to be highly satisfactory to management. For 1949, pension contributions were 5 percent of covered payroll and averaged $184.32 per participant. The average annual contribution of male participants ($194.23) was nearly twice as large as the contribution made on behalf of females ($104.55).

There were several reasons why this firm was pleased with the financial management of its plan. Pension trust fund earnings in all years were in excess of 2.5 percent per annum.[16] In one year the annual earnings rate was 2.9 percent. The pension liability incurred by reason of the years of service of employees in the Company before the founding of the plan was accelerated during good profit years (the World War II period and immediate postwar period) and was completely discharged within six years after adoption of the plan.[17]

Certain other company policies may account for this financial record. The firm has discontinued making large lump-sum payments to participants who qualify for small pension benefits. Instead, the company pays life annuities, thereby speculating somewhat on the life of the retirants. More cash, however, is retained in the pension trust fund and is available for investment purposes. Several members who have reached retirement age have been placed on extended service, thereby further reducing pension outlays. Finally, the company has amended the plan so that the maximum age at which employees may join the plan is age 53.[18] Formerly, it was age 65. This eliminates the potential expense of purchasing benefits for older "new" employees, who normally require proportionately higher contributions in order to provide a stated benefit.

of membership were required. Company B, a "selling" organization, had a larger proportion of high salaried executives in the organization, all of whom participated in the plan. (Actually, at Company A, the president was not eligible for membership. He excluded himself from membership in the design of the plan because through private arrangements he already had sufficient "insurance." He stated, moreover, that pension costs would be more manageable.) Age and sex differences among the members in the two plans were minor and not significant from the cost standpoint.

[16]In 1949, 56 percent of the pension trust fund was invested in government bonds, 28 percent in other bonds and mortgages, and 15 percent was invested in preferred and common stocks.

[17]Since the minimum allowable period for funding past service credit (for federal tax purposes) is ten years, annually not more than 10 percent of the total past service cost is deductible from gross income.

[18]Although this firm had no restrictive hiring practices, such as a maximum hiring age, a management representative agreed that this change in the plan may have a tendency to restrict employment to persons under age 50.

CHAPTER II

COVERAGE OF PENSION PLANS

The coverage of the pension plans in this study, and in general, varies widely from company to company, depending on whether all or only part of the employee group is included. Actual participation of the covered group may be further limited by age and service requirements.

Nature of Coverage

Generally, among firms operating pension systems, all full-time employees are eligible to participate in the plan.[1] However, some plans are set up so that they benefit only certain classes of employees, such as salaried employees (as distinguished from hourly paid employees). Such restrictions in coverage are justified by employers usually on the grounds that available funds are insufficient to cover all employees.

Actual participation of the covered group may be further limited by service and age requirements. The objective of the service qualification, customarily one to five years, is to eliminate the potential expense that may be incurred in making pension contributions on behalf of new employees, a group that normally has high labor turnover. Thus, pension contributions are made only on behalf of those persons who are expected to be "permanent" employees of the company. The justification for the use of the minimum age requirement, customarily age 25, 30, or 35, is similar to that used to explain the service requirement; it is commonly believed that youthful employees shift around before they finally establish "roots" in an organization. Use of maximum age qualifications, generally between age 50 and age 65, has two main reasons. In the first place, from a psychological standpoint, it is undesirable for a company to provide small benefits to retired employees. Apart from the poor public relations aspects, payment of small benefits has a poor effect on the morale of the work force. The cost of providing full pensions for older employees, on the other hand, is exceedingly high. Actually, it is difficult to fund any sort of retirement benefit for "new" older employees without making huge annual contributions, because there are no accumulations of pension reserves on their ac-

[1]Generally, companies do not grant part-time or seasonal employees, as defined by the Bureau of Internal Revenue, coverage in pension plans. Section 165 (a)(3)(A) of the Internal Revenue Code defines a part-time employee as one whose customary employment is for not more than twenty hours in any one week, and a seasonal employee as one whose customary employment is for not more than five months in any calendar year. Employees not within the scope of the Bureau's definition of part-time or seasonal employee are classified as full-time employees and are eligible for participation in plans.

counts, and contributions made on their behalf have little or no opportunity to receive interest.

Coverage of the Plans Studied

Seven of the eleven plans studied here, all employer-initiated, allow all employees to participate. Two other plans, both employer-initiated, cover salaried employees only. The two union-negotiated plans cover all employees in the bargaining unit, and one of these also covers all other company employees.

Except for the two negotiated plans, all of these plans have age and service requirements (customarily called eligibility rules) that further limit the size of the covered group. These nine plans require employees to complete a period of service, varying from one year to five years,[2] before becoming eligible to participate in the plan. Four of these plans require further that employees reach a certain minimum age, either age 25 or 30. All nine plans restrict participation after ages varying from 53 to 70.

The maximum eligibility age specified in these nine plans, however, is not the true maximum. The true maximum, beyond which participation is barred, is the maximum specified in the plan, less the period of service required. Table 1 shows that in two plans the service requirement reduces the maximum age for eligibility to participate by two years and in three other plans by as much as five years.

Table 1. **Effect of Service Requirement upon Maximum Age Requirement in Nine Employer-Initiated Pension Plans — 1950**

Company	Service Requirement	Maximum Age Requirement	"True" Maximum Age
A	3 years	55	52
B	3 yrs. 11 mo.	65	61
C	4 years	60	56
D*	2 years	70	68
E	5 years	55	50
G	5 years	55	50
H	2 years	60	58
J	5 years	65	60
K	3 years	53	50

*Service requirements in this plan were two years for hourly paid employees, one year for salaried employees.

Although there are no age or service requirements in two union-negotiated plans, a similar effect results from a 15-year service require-

[2]Section 165 (a)(3)(A), Internal Revenue Code, specifies that the maximum period of service cannot exceed five years.

ment for receipt of benefits. For example, assuming a retirement age of 70, employees hired after their 55th birthday will be ineligible for pensions.

Experience with Eligibility Rules

As a result of unprecedented labor turnover and changing employment patterns in World War II and the postwar period, eligibility rules have failed to meet their objective. Service and minimum age requirements were expected to confine participation to "permanent" employees. In many cases, however, this expectation was not fulfilled. The experience of two firms, Companies B and D, is illustrative. Both of these firms experienced unexpectedly large separations among male employees who had met minimum age and service requirements. On the other hand, youthful female employees who were not expected to become plan members, remained with the companies long enough to establish a short period of membership.

The basis upon which eligibility rules were developed seems to have no relationship to results attained. A majority of companies relied on crude estimates of their labor turnover. But, even where more refined methods were used, as in two cases, the difference between expected and actual experience was substantial.

Effects of Eligibility Rules and Other Exclusions on Participation

Among the eleven plans studied here, participation of employees varied widely. In six of the plans, more than 50 percent of the total work force did not participate. Arbitrary exclusions of various groups, restrictive age and service requirements, and employee unwillingness to participate explain the variations. The effects of these factors may be seen in Table 2.

Definition of coverage. Except in two instances, regardless of occupation or method of wage payment, all employees were included in the definition of coverage. In two companies, Companies G and H, the plans covered only salaried employees. As a result, approximately three fourths of the total work force in one case, and three fifths in the other, were excluded from participation.

Age and service requirements. Minimum age and service requirements excluded nearly half of the employees in four of the seven companies for which information was available. In one case, Company J, 58 percent of the total work force was ineligible to participate in the

Table 2. Extent of Nonparticipation in Eleven Pension Plans — 1950

Company	Reason for Nonparticipation (*Percent of Total Work Force*)				
	Definition of Coverage	*Age and Service Requirements*		Unwilling to Participate	Total
		Failure to Meet Minimum Age and/or Service Requirement	Failure to Meet Maximum Age Requirement		
A	0.0	17.5	8.0	0.0	25.5
B	0.0	39.0	0.0	1.1	40.1
C	0.0	48.2	0.0	3.1	51.3
D	0.0	44.8	0.0	3.4	48.2
E	0.0	76.9	0.0	0.0	76.9
F	0.0	0.0	0.0	0.0	0.0
G	60.0	NA	NA	0.0	60.0*
H	76.5	NA	NA	1.0	77.5*
I	0.0	0.0	0.0	0.0	NA
J	0.0	57.7	0.0	1.8	59.5
K	0.0	49.6	2.0	0.0	51.6

*Most of the total is accounted for by the definition of coverage; however, some salaried employees, otherwise eligible, did not participate because of failure to meet minimum age and service requirements.

plan because of failure to meet the minimum age or service requirement.

Actually, the service requirement was the most important rule for limiting participation in pension plans. In two cases, Companies C and D, the sole limitation imposed was service, and in both cases approximately 48 percent and 45 percent of the total respective work forces were ineligible to participate. In still another instance, Company E, a 5-year service requirement permitted less than a fourth of the employees to participate in the plan.

Employees restricted by service requirements, or minimum age requirements, in the normal case, if they remain with the employer, will eventually qualify for participation. However, a maximum age qualification — 50 years of age, for example — is particularly onerous from the standpoint of the employee who is aged 51 because failure to meet the requirement permanently bars participation.

At Companies A and K, the maximum age requirement was an important limiting factor. As much as 8 percent of the total work force in one case, and 2 percent in the other, were permanently barred from participation because of failure to meet the maximum age requirement.

Employee unwillingness to participate. Even though they may otherwise be eligible, some employees fail to participate in the pension plan. Among the eleven plans, there were five such cases. In two cases, over

3 percent of the work force voluntarily remained outside the plan. The degree of unwillingness to participate is particularly marked in one of these cases, Company D, which is a noncontributory plan.

Several reasons explain voluntary exclusions. Where plans are contributory, some employees claim that they are unable to make contributions because all wages received are needed to meet current living costs, while others consider benefits so small that membership is not worth while. Still other employees have deeply rooted prejudices against insurance of any kind, or feel that individual security measures obviate the need for "group" coverage. Another reason, particularly important in the case of noncontributory plans, is that employees dislike paying personal income tax on the employer's contribution.[3] The high percentage of voluntary exclusion at Company D is attributable chiefly to an administrative ruling that employees must submit completed applications within 30 days of notification; otherwise participation is permanently barred.[4]

[3]According to a ruling (P. S. No. 58 Revised March 7, 1947) of the Pension Trust Division, Bureau of Internal Revenue, where the employer pays a premium on life insurance protection provided for an employee under a retirement income contract held by an employee's trust, then, the employee must include in his income the term life insurance cost of the life insurance coverage provided under the policy. The amount of life insurance coverage per individual was determined by subtracting the cash value of the policy at year's end from the face amount of life insurance. The remainder was the actual amount of life insurance carried by the employee for the year. The premium rates used were the term insurance rates of the issuing insurance company. As an alternative the employer may use a schedule of term insurance rates promulgated by the Bureau of Internal Revenue. The Bureau's rates were as follows:

Premium per $1000 of Life Insurance

Age	*Premium*	*Age*	*Premium*
15	$1.27	40	$ 4.42
20	1.61	45	6.30
25	1.93	50	9.22
30	2.43	55	13.74
35	3.21	65	31.51
		60	20.73

[4]The company was considering an amendment to mitigate the harshness of this rule.

CHAPTER III

RETIREMENT POLICIES AND EXPERIENCE

This chapter describes and analyzes the retirement policies of eleven companies and, where available, experience with retirements. Generally, covered employees qualify for benefits by completion of a period of service or by attainment of a certain age, or both. Whether employees retire or continue in service when these conditions are fulfilled varies from case to case. In some cases, continued service is at the employer's discretion; in others, the employee exercises the option.

Some of the plans also provide for an early retirement benefit or a kind of disability benefit in lieu of a regular pension. Sometimes both are provided. Receipt of such benefits is generally contingent upon the satisfaction of certain service and age requirements. Incapacity must also be demonstrated for disability pensions. Since such provisions are similar to the service and age requirements for normal retirement, they will be discussed in that connection.

Conditions for Receipt of Benefits

Normal retirement. The attainment of age 65 qualifies participants in all eleven plans for normal retirement benefits. Participants who join after age 55 in three of these plans, and after age 60 in another, qualify at various later ages, ranging from age 65 to 70. Seven other plans give no particular consideration to older employees.

A stipulated period of service for the receipt of retirement benefits is required by only two plans, both of which are union-negotiated. The period of service required in those two cases is 15 years. The service requirement in the nine other plans is not stipulated but varies for each individual employee and from plan to plan. The age at which the employee enters the company's service, subject to age and service requirements for participation, determines the amount of service actually required for retirement benefits. At Company H, for example, an employee who joins the plan at age 25 must complete 40 years of service (until age 65) before he is eligible for benefits; an employee who joins at age 35 must complete 30 years, etc. Moreover, since a maximum eligibility age is contained in these plans, a certain minimum period of service — from maximum age for eligibility to normal retirement age — is required. Table 3 illustrates how this operates.

In nine plans, participants are expected to retire automatically upon

Table 3. **Minimum Service Requirement for the Receipt of Pensions in Nine Voluntary Pension Plans — 1950**

Company	Age at Joining	Normal Retirement Age	Minimum Years of Service Required
A	Age 55 or under	65	10 years
B	Age 55 or under	65	10 years
	Age 55–61	10 years after joining or age 70, whichever occurs earlier	9–10 years
C	Age 56 or under	65	9 years
D	Age 55 or under	65	10 years
	Age 56–68	10 years after joining or age 70, whichever occurs earlier	2–10 years
E	Age 55 or under	65	10 years
G	Age 55 or under	65	10 yeras
H	Age 55 or under	65	10 years
	Age 56–58	10 years after joining	10 years
J	Age 60 or under	65	5 years
K	Age 53 or under	65	12 years

attaining normal retirement age; extended service is discretionary with the managements involved. In the two union-negotiated plans, extended service is optional with the employee. However, if an older employee's physical capabilities decline so that his ability to perform work is impaired, the seniority provisions of the labor agreements give these employees some opportunity to press for retirement. Ability to perform usual duties, in the event of dispute, is determined by a union-management conference.

Early retirement. Two of the eleven plans provide for early retirement. Usually early retirement involves employees who have aged prematurely or whose capacity for further service is limited. Employees who retire early must have completed 15 years of service, and one of these plans further requires the attainment of age 55. But, in both cases, early retirement is subject to company consent.

Disability retirement. Both collectively bargained plans and one employer-initiated plan provide for disability retirement. Disability retirement is available in the negotiated plans only if the disability occurs after 15 years of service. Action for retirement may be initiated by either the employer or employee, and proof of disability must be established by the party initiating action. The other plan, a self-administered one, provides for such retirement, with company consent, if the disabled employee has completed at least 15 years of membership or has attained age 60. Although the other plans do not specifically provide for disability retirement, seven of them allow disabled members to take the accumulated cash value of company contributions on withdrawal, in addition to any cash values which they may have as a matter of right.

Definition of Service

In industry, the continuous service required of employees to qualify for benefits is interpreted liberally. Interruptions in service beyond the employee's control, such as temporary disability or involuntary layoff, normally do not incur a break in service for pensions, provided they do not extend beyond a certain period of time. Among the plans studied, the pattern of allowable breaks in service varies considerably.

All eleven plans continue pension credits despite temporary disability, layoff, leave of absence, and military leave. The allowable period of interruption is specified in nine plans. In the event of temporary disability, the allowable interruption ranges from six months to four years, with one and two years common. For layoff, allowable breaks range from three months to two years, with one and two years common. One union-negotiated plan preserves previous pension credits for two years in case of layoff. Additional credits, however, are limited to layoffs of one year or less. For leaves of absence, the allowable interruption ranges from three months to two years, with six months being the most common allowance. Military service during World War II was fully credited by all plans, provided the employee was re-employed within three months after discharge.

Except for three plans, employees who quit or are discharged forfeit pension credits. One employer-initiated plan, Company D, restores credits if rehire takes place within one year. Subject to negotiation, pension credits may be reinstated under two collectively bargained plans if rehire takes place within six months after resignation or discharge.

Considerations in Determination of Pension Qualifications

Qualifications for the receipt of pension benefits reflect the various purposes of the pension planners. There appear to be four common considerations. These considerations, however, were of varying importance to employers.

1. Since one of the usual purposes of plans is to eliminate superannuated employees, the retirement age of the plan must have some relationship to the date that superannuation occurs. This involves a consideration of industrial, occupational, and sex differences as well as differences as to particular individuals.

The age at which superannuation occurs among the various industries and occupational groups, of course, would not be expected to be similar because of the varying demands of different types of employments and the physical vigor of different individuals. Yet, in all plans studied employees are normally eligible for pension benefits at the same age, although the industrial groupings of these employers in some cases represent significant differences. In all plans, moreover, the same normal retirement age applies to the various occupational groupings covered by the plans. Several firms (Companies A, D, and F) employ large numbers of semiskilled machine operators; another (Company E) employs mainly skilled craftsmen; two other nonmanufacturers (Companies C and K) employ large numbers of clerical personnel; and two other nonmanufacturers (Companies G and H) cover salaried employees only. Furthermore, in all plans studied the same retirement policies apply to both the male and female employee, although three nonmanufacturers are large employers of females. Finally, a fixed retirement age that gives little or no consideration to individual variation in strength and vigor may create individual inequities. On the one hand, employees that age prematurely will leave the service of the company before they can satisfy conditions for pensions, and, on the other, some employees may be able to continue in employment beyond the retirement age.

2. Since the retirement plans are customarily expected to reduce labor turnover, qualifications for pensions are established so a certain age must be attained and a period of service rendered in order to receive benefits. As noted above, all firms established certain age and minimum service requirements as conditions for pensions. The expectation of pension benefits is an inducement to continued service, although the actual weight of the inducement has never been determined.

However, other pension plan provisions, such as vesting provisions, weaken whatever effect pension qualifications may have to continued service. In seven of the eleven firms studied, a member may terminate employment before he has satisfied the pension qualifications and still qualify for benefits. At Company D, for example, terminating employees receive benefits after only two years of membership.

3. Since all plans in operation when this study was conducted were funded plans, in order to estimate pension costs and to establish a contribution rate a retirement age had to be assumed. For funding purposes, age 65, with special consideration to older employees in four plans,[1] was selected as the normal retirement age in all plans.

[1]In three of those four plans, employees enrolled after reaching age 55, retired 10 years after joining the plan, or age 70, whichever occurred earlier. This modification was introduced primarily

Because the normal retirement age is customarily the terminal funding date,[2] it is clear why a lower retirement age was not selected. Lowering the retirement age five years to age 60 would increase appreciably the cost of the plans, perhaps as much as 50 percent. A policy of retirements at age 70, however, would substantially lower costs. Yet, no firm (except for special consideration for older employees in four cases) had such a policy.

Even in the case of the two union-negotiated plans, if these plans are to be funded, some retirement age will have to be assumed. Age 65 appears to be the logical choice because at that age employees become eligible to go on the pension roll. A complicating factor in funding the benefit, however, is that service after age 65 earns pension credit, and, since continued service is discretionary with the employee, the individual's actual retirement date is unknown.

4. Retirement age under the Federal Social Security program was an important consideration in determining the selection of a normal retirement age in all plans. In seven of the eleven plans, plan benefits were integrated with primary Social Security benefits; in four others, employers indicated that their private plans supplement Social Security. Since Social Security benefits become payable at age 65, the private company benefit (the supplement) also becomes payable at the same time.

Retirement Experience

Of the nine plans in operation as of June 1950,[3] six reported experience with retirements. At that date the two union-negotiated plans were not in operation. None had any experience with early or disability retirements. Four of the six firms reporting experience had individual annuity plans, another had a self-administered trusteed plan, and one had a group annuity plan.

Pension plan retirements. Four firms had actually retired employees automatically under their plans. The self-administered trusteed plan, in operation since mid-1943, as of December 1948 had 21 persons on the pension roll, each receiving an average private monthly benefit of

to increase the period of time over which pension contributions were made so that annual installments would not be too difficult to meet. In the other plan, Company J, employees age 60–67 in the work force at the time the plan was adopted were allowed to continue in employment for an additional five years or age 68, whichever occurred earlier. The main reason for the modification was to reduce the "shock" of retirement to employees, and to allow for the gradual release of "superannuated" employees.

[2]This means that employee pensions are expected to be completely paid for at normal retirement age and that no further contributions are required. Moreover, active service beyond the normal retirement age earns no additional pension credit.

[3]Six individual annuity plans were adopted during the period 1941–1943; the self-administered plan was adopted in 1943; the profit-sharing retirement plan was adopted in 1947; and, finally, the group annuity plan was adopted in 1948.

approximately $33 exclusive of OASI. Of this total of 21 pensioners, only three were added during the year 1948. In that year 10 employees reached retirement age; seven employees, however, qualified for such small benefits that the company preferred to pay them lump sums, thus eliminating them entirely from the pension roll. These lump sums averaged approximately $500 per person.

One individual annuity plan, in effect for seven years, retired two persons under its pension plan. Both employees attained age 70 in 1949 and were retired with a $10 monthly benefit. Another individual annuity plan, in operation since 1941, has automatically retired four participants. From May 1948 to December 1949 the group annuity plan had also made some automatic retirements at age 68. Details on the size of benefits were not available from either of these two companies.

For several reasons an automatic and uniform application of retirement policies to all retiring employees may be impractical, or at least difficult. Apart from the low benefits, cited above, employee unwillingness to face the inactivity of retirement and, in some cases, the existence of a group unable to qualify for any retirement benefits explain the difficulty. For example, Company J's personnel director remarked, "Employees just don't want to retire when they reach retirement age — they prefer to remain at their jobs." In two cases, Companies A and K (see Table 2, page 12), older employees representing 8 percent and 2 percent of the respective work forces will receive no pensions because of failure to satisfy the maximum age requirement for membership. In one instance, Company K, a dual policy that forced plan participants into retirement at age 65, and permitted nonparticipants to continue working beyond that age, further illustrates the problem with retirements. As a result, retirement policies in some firms are often modified so that the participant who reaches retirement age is continued in service.

Extended service. Extended service, in some cases, seems to depend primarily on the employer's current personnel needs. Most of the twelve employees eligible for retirement but continued in the service of Company K possessed needed skills, although other factors were undoubtedly important in some instances. For example, one of the company's grain buyers was retained in service five years beyond normal retirement age before a suitable replacement was obtained.

Informal retirements. In four of the nine plans[4] in operation at the time of this study, some employees could not qualify for the plan at

[4]In five other plans, at the time of adoption, all older employees qualified for participation.

the time of adoption because they were older than the maximum age for eligibility to participate. In two cases, special arrangements were made for such employees. Company A allowed a 70-year old employee to work three additional years and purchased war bonds on his behalf, valued at approximately $1,000, which he received as a lump sum at retirement. Company C permitted an older employee to continue in service beyond age 65, until the employee decided to retire. At retirement this employee received a small lump-sum benefit. In contrast with these cases, two other firms (one with a self-administered plan and the other with a group annuity plan), although they allowed older employees to continue beyond the normal retirement age, provided no retirement benefits of any kind. Thus, immediately following pension plan adoption, two sets of retirement practices were in effect in the four cases cited. One applied to participants and the other to nonparticipants.

Employer and Employee Views on Retirement Policy

There is no general agreement between employers and employees as to when actual retirements should take place. Moreover, employers themselves hold varying views.

Although two employers had identical retirement policies, they held opposite viewpoints as to who should determine retirement. Company I maintained that the management should have the right to retire employees at age 65, and that extended service be discretionary with the management. This firm claimed that under a policy of voluntary retirements the company would suffer a hidden cost through the retention of superannuated, less efficient employees.[5] Company F's president, on the other hand, was in complete accord with the policy of voluntary employee retirements after age 65. He remarked, "An employee may retire when he feels that he wants to retire. The individual worker is the best judge."

Even where retirements are discretionary with the management, in some cases it appears that employees will not be asked to retire when they reach their normal retirement age because employers are uncertain as to when superannuation occurs. The president of Company E, for

[5]In pension negotiations of Company I, the union presented the following four points in support of voluntary employee retirements: (1) Managerial determination of superannuation will usually be disagreeable to the individual employee because retirements, in many cases, will be "forced," and, moreover, individual employees will invariably blame the union for "forced" retirements. (2) Under the seniority provisions of the basic labor agreement, management has the right to relieve those employees who are physically unable to perform satisfactorily. (3) Voluntary employee retirements will reduce pension costs because the "average" age at which employees will retire will be somewhat higher than age 65, perhaps age 68. (4) Since service after age 65 will earn pension credit, individual employees with 10–14 years of service at age 65 will have an opportunity to continue in the service of the company until eligibility for pensions is established.

example, stated that retirement at age 65 will not be compulsory. "Just how long a man continues to work," he stated, "will depend entirely upon his physical condition. Each case of retirement will be different." According to this official, the employer in consultation with the individual concerned will determine a proper retirement age. In another case, the president of Company A stated, "Retirements will not be compulsory. Much will depend upon the individual's physical condition. The company and the individual concerned will work out a retirement age."

Several employers indicated that "actual" retirement age and normal retirement age are not the same. These employers have not evolved a definite retirement policy, the pension plan provisions notwithstanding. To them, the normal retirement age was a terminal date for funding purposes. It was a date beyond which the participant no longer accumulated pension credits, but one beyond which an employee could very well continue in employment. With other employers, however, retirements may be compulsory.

Company B, for example, which will have a large group of employees eligible for retirement in 1952, came to a tentative decision that a uniform retirement for all employees was the only practicable policy. "Putting retirements on an individual basis," Company B's treasurer stated, "will surely cause headaches. Some employees will be retained; others, however, will be retired. Retirements will be difficult to justify." In certain cases, moreover, preferential treatment will be alleged. According to Company B's representative, the only retirement policy not susceptible to misinterpretation is one of uniform retirements for all.

CHAPTER IV

PENSION PLAN BENEFITS

This chapter discusses the factors considered in pension benefit formula design, and describes and analyzes the benefit formula of the eleven plans studied. Types of benefits considered are normal retirement benefits, early retirement benefits, disability benefits, and death benefits. Since seven of these companies integrate plan benefits with primary Federal Social Security benefits, this aspect is also considered.

Factors Influencing Benefit Formulae Design

Pension benefit formulae are devised (1) to provide a benefit in some relationship to an employee's standard of living, (2) to provide a benefit in some relationship to the period of service with the company, and (3) to provide benefits large enough so that they serve as an inducement for superannuated employees to leave the service of the company. The considerations listed below are of course modified by the company's ability to pay for pensions.

1. Pension benefits, within limits, are usually related to the earnings of the individual. Since a standard of living depends normally on wages received, relating benefits to wages tends to maintain the standard. Usually, pension benefits are only a proportion of the worker's wage; however, the pension paid to all employees normally bears a constant relationship to the worker's wage. In ten of the eleven plans studied, wages earned by members were a factor in determining the amount of benefits paid.[1] The other plan gives no consideration to wages paid.

Employers, generally, accept the concept of relating pension benefits to an employee's wages. Several employers indicated, moreover, that an "adequate" minimum pension should be paid. The comments of two employers are illustrative.

Company G's president stated, "Benefits after retirement should be scaled to earnings. The executive with large earnings should receive a larger pension than one granted a lower paid wage earner, because he may have debts, obligations, and a pattern of life that differs from that of the wage earner. However, both should greatly reduce their cost of living at retirement." In another case, Company E's president remarked, "The company should see to it that the employee has a rea-

[1]There is some modification of this concept in that five firms impose a maximum limitation on benefits, and seven pay minimum benefits to all members.

sonably comfortable level of living at retirement. It should not be 'too large.' It should be 'adequate.' "

2. Stimulus to long service with the company is gained by using the period of employment as a factor in calculating benefits. With some limitations,[2] in six of the eleven plans studied, the longer the period of service, the larger the pension benefits received. The other five firms give no particular consideration to long service.

Comments of two management officials illustrate employer views on the relationship of benefits paid to service with the company. Company F's treasurer indicated that the management visualizes pensions as a reward for long service. In another case, the president of Company E stated, "The company's responsibility to the employee in the matter of pensions is in direct proportion to the service rendered. The company's obligation is less when the service is less. Longer service with the company should result in higher benefits."

3. In order to eliminate superannuated employees, the benefit level must be high enough to induce employees to retire. Seven of the eleven plans studied here provide "minimum" benefits; in five plans, the minimum benefit is a stated percentage of compensation, and, in two others, a flat minimum benefit is paid. Four other firms, however, do not guarantee any minimum pension.

The employers in this study held no common opinion as to the size of benefits necessary in order to induce superannuated employees to retire. Company H's treasurer suggested, for example, that his company's $100 monthly minimum pension is adequate. He remarked, "The company would not adopt a plan with inadequate benefits. The idea of scaling benefits so low that management can carry the premiums during slack periods has apparent disadvantages. The benefits will be too low." On the other hand, Company F's treasurer stated, "The present level of pensions ($100 monthly) is inadequate to affect retirements satisfactorily."

Although the amount of pension benefits and benefit formulae, generally, reflect the various objectives of pension plans, where a "suitable" benefit, or a type of benefit is in direct conflict with costs, a modification in design is usually made. General factors, such as economic conditions, and particular factors, such as the market position of the individual firm, influenced all employers in making a decision as to the company's ability to provide a certain level of benefits.

[2]The limitations are (1) no credit for service beyond 25 years of service in one plan, (2) no credit for service past age 65 in two plans, (3) no past service credit beyond a stated maximum in one plan, and (4) no credit for service rendered prior to date of enrollment in four plans.

The following evidence shows the importance of cost considerations in determining the level of benefits and the benefit formulae in pension plans. The company's "ability to pay" was the chief factor in the determination of the level of benefits and the benefit formula at Company I. This major issue was resolved in favor of the management, when the union's proposal for the Bethlehem Steel[3] formula was rejected by the company, and flat $100 monthly pensions were agreed upon by the parties. In another case, Company F's president stated that the cost assumed under the union-negotiated plan was not in accordance with the company's ability to pay. Objecting to the union's application of the Bethlehem Steel pattern to his plant, he stated, "No consideration was given to the individual financial situation of the company or the ability of the company to continue to meet pension payments in all sorts of economic climate."

Normal Retirement Benefits

The eleven plans studied incorporate five of the benefit formulae used commonly today. The benefit formulae include flat percentage, unit, money-purchase, flat amount, and money-value. How well these benefit formulae further the objectives of the plans is the major interest of this section. Criteria for judging the formula, cited below, include relationship of benefit to wages and accustomed living standards, relationship of benefits to length of service, amount of benefits, and effect of formulae on pension costs.[4]

Flat percentage of compensation. Five pension plans, all of which are individual annuity plans, use the flat percentage of compensation benefit formula. This formula provides an amount equal to a certain percentage of the employee's compensation as of a specific date, normally five years prior to normal retirement age. Three plans provide a benefit equal to 40 percent of compensation; one provides 36 percent of compensation, and the other provides 60 percent of compensation. Compensation does not include overtime and, with one exception, does not include bonuses and commissions. Earnings in the fifth year before retirement are the basis on which the benefit is calculated. Wage changes in the next five years of employment have no influence on

[3] *Agreement between United Steelworkers of America, CIO, and Bethlehem Steel Company.* Oct. 31, 1949, p. 5. This agreement must be read in connection with the Pension Plan of the Bethlehem Steel Corporation and subsidiary Companies, adopted Jan. 25, 1923, as amended to July 30, 1948. (The benefit formula is described on page 26, in this bulletin.)

[4] Since benefits depend upon certain conditions outside the scope of the plan itself, such as wages paid, the benefit formula does not set an absolute limit on costs. Nevertheless, by establishing fixed standards, such as benefit ratios (or contributions), and by specifically defining the years of service (or the amount of wages) that incur pension costs, certain cost controls are established.

benefits. In all five plans, the primary Social Security benefit is deductible.

The formula fails to satisfy most of the criteria set forth previously. In the first place, the formula fails to reward long service. For example, Company D's controller remarked, "If two employees receive the same wage, they will both receive the same retirement benefit. It makes no difference if one employee has 25 years of service and the other has only 10 years." The formula also requires extremely high rates of contributions in order to finance benefits for older employees. Experience from Company B's plan is illustrative. This firm is paying an annual premium of $509.46 in order to provide a $30 monthly company benefit, due at age 65, for a male employee age 56. Only $98.56, on the other hand, is being paid annually to provide a $35 monthly company benefit for a male employee age 27. Differences in contribution rates such as these may lead to restriction of employment opportunities for the older worker.

The formula complicates the administration and financial management of the plan. Because of the method of funding used, expected benefit liabilities must be recalculated as wages change. Since all plans are individual annuity plans, this also means that additional contracts must be purchased. Moreover, in the case of older workers, purchase costs increase disproportionately with age.

In noncontributory plans, the company contributes a larger portion of the benefit provided for high paid employees than for low paid employees. For example, if the plan benefit equals 40 percent of compensation, the company contributes only 33 percent of $1,440, the total pension of an employee earning $3,600.[5] The remaining 67 percent comes from joint contributions under the Federal Social Security program. On the other hand, for an employee earning $9,000 annually, the company purchases 73 percent of the total benefit of $3,600.

The benefit formula is also intended to maintain some relationship to the cost of living. However, as was pointed out previously, wage changes within five years of the normal retirement age have no effect on final benefits. Yet, in periods of rising prices, five years can produce significant changes in the cost of living. For example, the Consumers' Price Index, during the period 1946–1951, rose 23 percent.[6]

Unit-benefit formula. Two plans using the unit-benefit formula pro-

[5]In this example, one assumption is made, namely, that both employees will qualify under the "new start" provisions of the *Social Security Act Amendments of 1950* for the full maximum primary Social Security benefit of $80 monthly.

[6]*Monthly Labor Review*, Table D-1, Consumers' Price Index for Moderate Income Families in Large Cities, by Groups of Commodities, July 1951, p. 118. The Consumers' Price Index, which for "all items" averaged 139.5 in 1946, was 171.9 in 1950.

vide a pension equivalent to a definite percentage of income for each year of service. One union-negotiated plan follows the Bethlehem Steel formula.[7] Pensions are equal to 1 percent of the average annual earnings of the 120 months preceding retirement, multiplied by the total years of service. Overtime and other extra compensation are included in determining average annual earnings. Past service and future service receive equal consideration. The benefit formula notwithstanding, employees with 15–25 years of service qualify for a minimum pension, including Social Security, of $4 for each year of service. The minimum pension benefit for employees with 25 or more years of service is $100.

The other plan, a self-administered trusteed plan, provides benefits for both future and past service but differentiates the two. Future service benefits cumulate annually at a rate equal to ¾ of 1 percent of the first $3,000 of annual compensation, plus 1½ percent on the excess. Past service benefits are 1 percent of compensation multiplied by the number of years of past service, but the first three years of service and service before age 25 are excluded. The basis of compensation for both past and future service excludes bonuses and special pay and, in the case of past service benefits, overtime as well.

In general, this formula adequately meets two of the criteria previously mentioned. Pensions are directly related to service, and, insofar as wages are a factor in calculating benefits, recognition is also given to different standards of living.

Although the formula is adequate in those respects, it has certain other deficiencies. Benefits require proportionately larger contributions for older employees, because there is less time to accumulate reserves. Since benefits are related to service, short-service older employees receive small benefits, and, in one case, employees with less than fifteen years of service at retirement are ineligible for any pension. In two of the cases studied here, other deficiencies resulted from modifications in the basic formula.

The self-administered trusteed plan illustrates a deficiency resulting from unequal treatment of different levels of compensation. In that plan, the formula applied to future service benefits provides proportionately more for the higher paid employee. An employee earning $3,000 annually for 25 years will qualify for a retirement benefit of $562.50, or approximately 18 percent of the average annual wage he received during employment. For an employee with similar service earning $9,000, however, the annual retirement benefit is equal to

[7]*Agreement between United Steelworkers of America, CIO and Bethlehem Steel Company.* Oct. 31, 1949.

$2,712.50 or approximately 30 percent of the employee's wage. When social security benefits are added, however, the percentage of wages is more nearly equal.

The union-negotiated plan is an example of the effect of a limited base period in the later years of working life on the financial stability of the plan. Since benefits in this plan are based on compensation for the 120 months preceding retirement, rising wage levels may make existing reserves inadequate and may require substantial additions in order to meet wide differences between expected and actual benefit levels.

Money-purchase benefit formula. Benefits are provided in two plans through the use of the money-purchase formula. The formula provides that an amount be credited each year toward the purchase of pensions. Although this formula does not customarily credit past service, this factor is involved in both plans. In one, an individual annuity plan, 5 percent of the employee's compensation at the time he enters the plan is deposited each year toward the purchase of a pension at retirement. Compensation does not include overtime, bonuses, commissions, or other forms of remuneration. Employees who became participants when the plan was adopted received $1 monthly pension credit for each year of past service. Since the plan requires a 3-year service period of new employees, at retirement $3 are added to their monthly benefit. The benefit formula of the profit-sharing retirement plan credits an annual distribution of company profits to the purchase of pensions. Credits are allocated on the basis of one unit for each $100 of annual compensation, and one unit for each year of past service. Compensation does not include overtime; the status of other forms of compensation is unknown.

One of the major shortcomings of this formula is that it provides relatively small retirement benefits for the older employee. The president of Company G remarked, "Personnel who are close to retirement will only be eligible for small benefits and may be reluctant to retire." In the other plan, 5 percent of a worker's wages will not buy substantial benefits when, for example, only ten years are available in which to make contributions. At Company A, 5 percent of wages over a funding period of ten years purchased a $6 monthly future service benefit for four older employees, a $9 benefit for another older employee, and, finally, a $24 monthly future service benefit for another senior worker. Even though this firm added a past service benefit to the future service benefit, the total monthly benefit provided for these six employees, all aged 55 and over, averaged $26.

From the management standpoint, the financial stability afforded by this formula is an outstanding advantage. Although the dollar amounts of contribution vary from time to time, pension costs never exceed a fixed rate. The pension benefit is the only variable. Company A's pension contributions, with some allowance for past service costs, remain constant at approximately 5 percent of covered payroll. On the other hand, although Company G's dollar contribution varies with profits, the annual rate of contributions cannot exceed 15 percent. The size of the shares depends upon the size of the employer's total contribution.

When wages rise, the money-purchase formula of Company A creates an inequity between younger and older employees. At that company, if an employee's compensation increases in the latter years of service, the amount of his annuity will not increase proportionately because of the higher costs of providing benefits for the older ages. Sizeable wage increases are required to buy a $10 additional monthly annuity, the smallest purchasable under the plan.[8] For example, gross annual premium rates quoted by a low-cost commercial insurance carrier show that, at age 45, twenty annual payments of $78.91, or an average annual wage increase of over $1,500, are required to purchase a $10 monthly benefit. For younger employees, however, as compensation increases, the amount of annuity will increase more rapidly because of the lower premiums necessary to provide benefits for the younger ages. At the time of this study, at Company A, the age group 30–34 qualified for average monthly benefits of $47, while the employees in the age group 50–54 qualified for only $29.

Flat-benefit formula. One collectively bargained plan provides benefits through the use of the flat-benefit formula. Benefits, under this formula, vary with service; wages, on the other hand, have no influence in the benefit computation. All retiring employees with 25 years or more of service receive a pension of $100 per month. For employees with service ranging from 15 to 24 years, monthly benefits are calculated at the rate of $4 for each year of service. Primary Social Security benefits are deductible from all benefits provided by the plan.

The emphasis on service and the elimination of wages in the computation of benefits open this formula to two criticisms. In the first place, the relationship between service and size of benefits is limited to a relatively short period of time. Benefits vary with service between the 15th and 24th years of service, but service after 25 years earns no further

[8]Underwriting rules of insurance companies, generally, require that the minimum purchase of an individual annuity policy be at least a $10 monthly benefit. A few companies, however, allow a $5 minimum purchase.

credit. In some cases, moreover, additional service may be necessary to meet the age qualification for retirement. In the second place, benefits bear no relationship to differences in individual living standards. Pensions are proportionately larger for the lower wage groups, assuming that their service equals the service of the higher wage group. For example, employees earning $2,400 annually qualify for an annual pension of $1,200, equal to 50 percent of wages, while employees earning $3,600 annually qualify for the same annual benefit, but this amount is only equal to 33 percent of wages.

Money-value benefit formula. The money-value benefit formula provides an annual benefit defined as a stated ratio of the amount of employee contributions. Although employee contributions are a fixed percentage of compensation, different rates apply to different parts of compensation. The usual dividing line is $3,000. None of the pension plans studied here uses this formula exclusively, but one group annuity plan calculates future service benefits through the use of the formula. Future service benefits, in this plan, are equal to one third of the total contributions made by the employee during his participation. Employees contribute 3 percent of the first $3,000 of their annual earnings, and 6 percent of earnings on the excess. The annual base rate of earnings does not include overtime or other extra compensation.

This formula has two shortcomings, the first of which is the absence of provision for past service credit. As in the two cases discussed under the unit-benefit formula, other provision had to be made by the group annuity plan to credit past service. The company provides past service benefits for employees, age 35–59, who became participants on the date the plan was adopted. These benefits are credited at the rate of 1 percent of the monthly earnings as of date of adoption, multiplied by years of service, and subject to a maximum of 10 percent of monthly earnings, or $62.50. Employees, age 60–67, who joined the plan on date of adoption, were provided with severance benefits in lieu of past service benefits. These benefits varied from $250–$1,000, depending upon age.

The second difficulty is that employees in the higher age brackets receive proportionately higher benefits than those provided for other employees because high wage employees are given an opportunity to make larger pension contributions. An employee earning $3,000 annually, at a 3 percent rate of contribution, contributes $90 annually. After 25 years of service, his total contribution is $2,250, which provides an annual benefit of $750, or a pension equal to 25 percent of the employee's average annual wage. On the other hand, an employee earning $20,000 annually contributes $1,110. After 25 years of service, the total contribution is $27,750, which provides an annual benefit of $9,250 or a pension equal to 46 percent of the employee's annual wage.

Benefit payments. All eleven plans pay normal retirement benefits for as long as the pensioner lives. Seven plans also guarantee a minimum cash amount to all pensioners. Six individual annuity plans guarantee a minimum of 100–120 monthly payments, representing approximately 75 percent of the cash value of the policy at retirement. The contributory group annuity plan, on the other hand, guarantees benefits at least equal to the employee's total contribution.

Nine plans, all employer-initiated, also offer certain payment options at the time of retirement. A joint and survivor option is available under all of these plans. Six individual annuity plans, moreover, provide further alternatives, such as cash refund annuity or deposit of the policy as an interest-earning capital sum. Two union-negotiated plans, on the other hand, leave pensioners with no alternative but to take a life annuity.

Other Benefits of Pension Plans

Not infrequently, when an industrial pension plan is adopted, other benefits, such as early retirement, disability and death benefits, are offered. Most of the eleven plans studied here provide one or more such benefits. Only two plans provide early retirement benefits; disability retirement benefits are available in ten of the eleven plans; and eight plans provide death benefits. These variations are largely explained by the differences among the plans with respect to the method of funding used. All three benefits, for example, are provided by only one, an individual annuity plan which uses the level premium accumulation method of funding.

Early retirement benefits. Only two of the eleven plans pay early retirement benefits. The group annuity plan pays benefits equal to the value of the normal retirement benefit discounted for death and interest.[9] The other, an individual annuity plan, provides a benefit equal to the accrued cash value of the individual's policy, at the time of early retirement. Payments begin immediately in both cases.

Both formulae have two related deficiencies. Benefits are inadequate because the period over which contributions are made is shortened by early retirement while, on the other hand, the benefit payment period may be lengthened. The effects of both factors can be illustrated by the

[9]This concept is customarily referred to as the actuarial equivalent.

individual annuity plan. If an employee enters that plan, at age 35 and his monthly pension benefit due at age 65 is $50, upon early retirement at age 50, the cash value of his policy would be sufficient to purchase only a $14 monthly benefit.

Disability benefits. The size and terms of the disability pensions available from ten firms vary from plan to plan. Two union-negotiated plans pay flat $50 monthly benefits. Payments start six months after disability is established. If an employee qualifies for both disability and normal retirement benefits, he receives the latter, which will always be the larger of the two. The self-administered trusteed plan offers disabled employees, with 15 years of service, benefits equal to 50 percent of the actuarial equivalent of the normal benefit, plus 5 percent for each additional year of service. With 25 years or more of service, or at age 60, disabled employees receive 100 percent of the actuarial equivalent of the normal benefit. Employees may elect to receive such benefits as immediate pension payments, or may defer payments until normal retirement age.

Because of the method of funding used, seven other plans allow disabled employees to take the cash value of accumulated contributions at the time disability occurs. Six of these are individual annuity plans; the seventh is a profit-sharing retirement plan. Subject to employer consent, various modes of payment are available, including lump-sum payment. Thus, since the cash values increase as the members age, and also with the probability of disability, these methods of funding provide a kind of disability benefit.

Just as in the case of early retirement, disability benefits are similarly low. In all but two plans, the formulae reduce the benefit by an amount proportionately greater than the difference between the normal retirement age and the age of disability. Under the self-administered plan, for example, an employee retired because of disability at age 60, with 25 years of service and a $3,000 annual salary, receives a monthly disability pension of $31, whereas at 65, his pension would then be $51, plus Social Security. Since Social Security benefits are not available until age 65, disability and early retirement pensioners are at a disadvantage because only one source of pension income is available.[10]

Death benefits. Nearly all firms studied here provide, under separate programs, group life insurance for their employees. The pension plans of eight of the eleven firms supplement this coverage with death bene-

[10]The Social Security Act Amendments of 1950 provide a new category of public assistance, namely, "aid to the permanently and totally disabled," from which some supplementation of low private disability benefits may be granted on the basis of need.

fits in cases where death occurs before normal retirement age. Six are individual annuity plans; one is a group annuity plan; and the other is the profit-sharing retirement plan.

The death benefit provisions of five individual annuity plans include a life insurance feature. All of them use retirement income contracts which require employees to pass a physical examination. Retirement annuity contracts are purchased for employees who fail to pass the examination.[11] A sixth individual annuity plan, on the other hand, provides only retirement annuities. The other two plans contain no life insurance feature, but return varying amounts of the contributions accumulated at the time of death. The contributory group annuity plan provides a death benefit that cannot exceed the sum of the employee's contributions, plus interest at 2 percent. The profit-sharing retirement plan returns the entire value of the accumulated cash contributions.

Pension Plans and Increased Social Security Benefits

Although the Social Security Act Amendments of 1950 were not yet in effect, most of the companies studied were considering the impact of any increased Social Security benefits on the financing of their plans. Seven of the eleven plans integrate plan benefits with primary OASI benefits. Since the private benefit purchased under these plans represents the difference between the total plan benefit and the individual's Social Security benefit, increases in Social Security benefits would disturb the existing relationship.

Five of the seven employers expected to utilize any increase in Social Security benefits, not to increase the total benefit but to produce a saving in the company's share of the total benefit. The remaining two firms, however, were apprehensive of such action because of a possibly unfavorable effect on employer-employee relations.

In one of the two latter firms, Company D, the controller indicated that the union may request that savings in pension costs be passed on to employees in the form of a wage increase. Moreover, he stated that since the pension plan was not within the scope of the collective bargaining agreement, the company was reluctant to make any move that may bring about pension bargaining. In the other firm, Company B,

[11]The retirement income contract provides a flat amount of life insurance, usually $1,000 for each $10 of the monthly annuity benefit. A member with a $29 monthly annuity benefit, for example, carries $2,900 of life insurance coverage. The retirement annuity contract, on the other hand, provides a death benefit equal to the cash surrender value of the contract at the time of death. When the cash value of the retirement income contract exceeds the flat amount of life insurance, both the retirement income contract and the retirement annuity contract have approximately the same death benefit, which is the cash surrender value of the contract.

it was possible that any improvement in Social Security benefits might become an additional benefit to employees. According to the pension consultant, the precedent for such a move is the General Motors Corporation-United Auto Workers[12] pension agreement which gives consideration to any improvements in Social Security benefits. Furthermore, he remarked that, by allowing the liberalized portion of Social Security benefits to remain to the credit of employees, the average level of benefits at Company B would be $100 monthly, the "standard" minimum pension customarily demanded by some large industrial unions.

[12]The General Motors Corporation-United Auto Workers, CIO, "Supplemental Agreements Covering Pension Plan and Insurance Program," dated May 29, 1950, commits the company to pay as its share of the total pension benefit, regardless of Social Security payments, not less than $1.50 per month for each year of service up to 30 years of service.

CHAPTER V

WITHDRAWALS, VESTING, AND MEMBERSHIP EXPERIENCE

Most terminations of employment are usually for reasons other than retirement, disability, or death. When such separations occur under contributory plans, employee contributions are returnable. Some plans, regardless of the source of contributions, also provide for payment to separating employees of all or part of the contributions made for them by their employer. This feature is termed "vesting." Vesting is usually contingent upon an employee's period of service with the company and, in some cases, on age. The mode of settlement varies from plan to plan, depending primarily upon the method of funding employed.

Most of the major pension plans, such as those negotiated in the auto and steel industries, do not include vesting provisions. The two union-negotiated plans studied here follow that pattern. Seven other employer-initiated plans, however, provide for vesting. This chapter describes the vesting provisions of these plans and analyzes the withdrawal experiences of all plans for which information was available. Since this chapter completes the analysis of pension plan benefits, the total membership experience, where available, is also considered.

Vesting Provisions

The seven plans that provide vesting include five individual annuity plans, the group annuity plan, and the profit-sharing retirement plan. Provisions of these plans, however, vary with respect to amount vested, period of service required, and mode of settlement.

Four individual annuity plans and the group annuity plan provide full vesting upon separation. Three of the four individual annuity plans, however, superimpose a service requirement for vesting of 2 to 10 years on a basic membership requirement ranging from two to four years. The other individual annuity plan requires employees to complete four years of service before they may participate in the plan and grants full vesting only after that requirement is met. In contrast, the group annuity plan grants full vesting only after 15 years of service have elapsed; 5 of these represent the initial membership requirement for plan participation; 10 years represent the vesting requirement.

The two remaining plans provide graduated vesting. The proportion of the employer's contribution received at separation varies with service. After five years of service, employees become members of the profit-sharing retirement plan and acquire a 20 percent vested right; each subsequent year of service is credited with an additional 4 percent. Service in one individual annuity plan also results in a vested right of 4 percent; the two-year service requirement for membership, however, is credited at an annual rate of only 3 percent. Normally, full vesting is attained after 26 years of service, but a supplementary provision allows members age 60 or over to separate with full vesting irrespective of their years of service.

Several modes of settlement are available among these seven plans. All five individual annuity plans permit the withdrawing employee to keep his policy in force at his own expense; alternatively, the policy may be surrendered to the insurance carrier for either a cash lump-sum payment or replacement by a paid-up annuity, maturing usually at retirement. The contributory group annuity plan only provides a paid-up annuity, contingent on all contributions remaining with the fund. Although a separating employee may withdraw his contributions, his right to any employer contribution in that event is forfeited. The method of funding sets no limit on the disposal of the vested cash sum under the profit-sharing retirement plan, but the pension committee can prescribe any particular mode of settlement.

Withdrawal and Vesting Experience

Some experience with withdrawals was obtained from five of the nine firms with plans in operation as of June 1950.[1] Complete history of withdrawals (approximately six to eight years of experience) was obtained from four vested individual annuity plans; aggregate data for only one year were obtained from the self-administered plan, which is nonvested.

Withdrawal experience. On the basis of the limited experience described below, no clear pattern of association emerges between withdrawal experience, on the one hand, and either provisions for vesting or the composition of the work force, on the other. It is probable that variations in withdrawal experience among these plans are more closely related to other factors, such as personnel policy and the behavior of the labor market, which are outside the scope of this report.

Withdrawal rates differed from plan to plan. In 1949, in Company K's nonvested plan, which has a 3-year service requirement for participation, members withdrew at the rate of 11 per 100. In contrast, during

[1]The two union-negotiated plans were not then in operation.

the same year, at Company B, where full vesting is permitted after four years required for membership, six members withdrew for each 100 participants. Although this contrast suggests that nonvested plans are more favorable to labor mobility, the even wider variations among vested plans lends no support to such a conclusion. In Company A, for example, which grants full vesting after five years of service (three years of service for participation and two for vesting) members withdrew at the rate of only 2 per 100 while at Company D, which has somewhat similar service requirements for participation and vesting, employees withdrew at the rate of 12 per 100 members.

Nor do factors, such as age and service, explain adequately the variations in withdrawal rates. Approximately six to eight years of experience of four individual annuity plans seem to show that low withdrawal rates are associated with high average age of membership. The average age of membership in two plans, annually averaging 5 withdrawals per 100 members over a 7-year span was approximately 45 and 46, respectively. Two other plans averaging 10 withdrawals per 100 members annually over the same period had average membership ages of 38 and 40, respectively. This relationship between withdrawals and the age of membership is weakened, however, by a further analysis of withdrawal ages. Of the four firms examined, the plan with the highest rate of withdrawal also had the highest average withdrawal age, namely age 40. Another company with a similar withdrawal rate had the lowest average withdrawal age (age 36) among the four firms.

A major component of all withdrawals was the short-service member. In three cases examined the average service of withdrawing members over approximately a seven-year span ranged from four to six years. In another case, however, employees averaged thirteen years of service at time of withdrawal. The experience of all four firms shows, moreover, that the short-service member is frequently also female.

Cost aspects of vesting. Vesting adds to the costs of providing for retirement because it establishes a claim against the fund for a larger number of persons. The costs of vesting vary in accordance with the terms of the plan. Data on costs were available from only two of seven plans, but they illustrate the effects of different vesting provisions. Both of these plans are individual annuity plans.

Company B's pension plan provides full vesting after the four years of service required for participation. During seven years of plan operation from December 1942 to December 1949, the average cost of each withdrawal was $650. The average premium outlay for withdrawing males was $1,000; for females it was only $180. Since all employee credits were vested in full, the employer recaptured none of these payments. Total benefits vested in withdrawing employees represented approximately 10 percent of the total premium outlay over the 7-year period of operation.

Company A's plan, on the other hand, does not provide vesting until after two years of participation, or five years of employment with the firm. Premiums paid on behalf of nonvested withdrawing employees revert to the plan in full, less the surrender charge of the insurance carrier.[2] Since a large proportion of the withdrawals in six and one-half years of operation was among short-service employees, one third of the average net premium of $330 paid on behalf of such employees was recaptured. Company A's average withdrawal cost, therefore, was only $220. Total benefits vested in withdrawing employees represented approximately 3.5 percent of the total premium outlay over the period.

Modes of settlement. Modes of settlement under vesting provisions are an important index of how closely the plans adhere to the objective of providing retirement security. Where vested rights are not available, it is clear, retirement income is available for only those employees who remain with the employer. Vesting provisions, on the other hand, do not exclude the possibility that pension benefits will not be available at the time of retirement for employees who terminate employment at an early age, but the plans are differentiated with respect to other modes of settlement open to such employees.

Only one of the seven plans permitting vesting, Company J's group annuity plan, restricts the mode of settlement to a paid-up annuity, which matures at the employee's normal retirement age. Although paid-up deferred annuities are available under the vesting provisions of five individual annuity plans and the profit-sharing retirement plan, the existence of other options does not assure an income at retirement. Moreover, even where paid-up annuities are issued at withdrawal, employees may exchange them for cash at any time.

The extent to which employees surrendered paid-up annuity policies for cash could not be determined for all plans. In the opinion of various consultants and plan administrators, most employees surrender their policies for cash. According to the controller of Company D, for

[2]In individual annuity plans, the cash surrender charges levied by the insurance carrier vary greatly, depending primarily upon the number of years the policy has been in force. The charge represents the difference between net premium outlay and cash surrender value. On members under age 45, the surrender charges on policies in effect less than 10 years may range from 10–50 percent of net premiums paid. At Company A, for example, total premiums paid on behalf of a plan member for a 7-year period came to $2,819. Had the policy been cash surrendered, the carrier would have returned only $2,452, or 85 percent of premiums paid. If a member withdraws within one year, some insurance companies retain the entire first year's premium.

example, all but a few of the twenty-nine employees who withdrew with full vested rights surrendered their policies for cash. At Company A, four of the five withdrawing employees surrendered their policies for cash amounts averaging approximately $400.

The practical effect of optional modes of settlement, such as those illustrated above, is to provide, for many employees, a system of deferred wages. The amount paid varies with age, length of service, and the past wages of the withdrawing employee.

Total Membership Experience of Four Selected Plans

Complete membership experience was obtained from only five companies; moreover, because of the small numbers involved in one plan, the data of only four plans are used in the analysis.[3] Table 4 summarizes the experience of the four firms.

Table 4. **Disposition of All Members of Pension Plans of Companies A, B, C, and D Who Were at One Time Participants in the Plan — 1950**

Period covered by analysis	(July 1943) (Dec. 1949) (6½ years)		(Dec. 1942) (Dec. 1949) (7 years)		(May 1942) (May 1950) (8 years)		(Dec. 1941) (Dec. 1949) (8 years)	
	Company A		*Company B*		*Company C*		*Company D*	
	No.	*%*	*No.*	*%*	*No.*	*%*	*No.*	*%*
Total enrollment in plan during the period	89	100.0	163	100.0	78	100.0	160	100.0
Deceased	8	9.0	7	4.3	1	1.3	1	0.6
Retired	0	0	2	1.2	0	0	0	0
Withdrew	17	19.1	41	25.2	35	44.9	73	45.6
Vested	(5)	(5.6)	(41)	(25.2)	(5)	(6.4)	(29)	(18.1)
Nonvested	(12)	(13.5)			(30)	(38.5)	(44)	(27.5)
Remain in plan	64	71.9	113	69.3	42	53.8	86	53.7

Private pension plans do not provide any retirement security for a substantial portion of members that at one time participate in them. Table 4 shows that nonvested withdrawals at three firms, Companies A, C, and D, were approximately 13 percent, 38 percent, and 27 percent, respectively, of the total membership group. Even where members withdraw with vested rights, they normally surrender their policies for cash, thus making no provision for retirement. Therefore, private pension plans provide retirement security only for those employees who remain with an employer until retirement age.

Actually, less than one out of every two employees who at one time

[3]Of the six other firms, three reported incomplete experience, one reported no experience; the two union-negotiated plans were not yet in operation as of June 1950.

participate in a private pension plan will remain with an employer and qualify for retirement benefits. Eight years of experience at Companies C and D show that only 54 percent of the total membership group for that period may still qualify for retirement benefits. The proportion that will ultimately qualify for retirement benefits is difficult to ascertain. However, it appears certain that less than one out of every two members will qualify, and subsequent experience may show that only one out of three or one out of four remains until retirement age. The experience of Company A suggests that somewhat larger proportions of the work force may ultimately qualify for pensions. However, the finding, in this case, is based on only six and one-half years of experience.

Six and one-half years to eight years of experience at Companies A, B, C, and D show that only one firm has a pension roll. As noted above, at Company B, two employees reached age 70 and were retired.

Postponing retirements, normally until 10 years after the date of adoption, in order to accumulate pension reserves explains the absence of pensioners: In all four cases, employees age 55 and over who became members on the date of adoption were continued in service for 10 years, or age 70, whichever occurred earlier. Employees under age 55 retire at age 65. Thus, in the normal case, at least a 10-year period is available for the accumulation of pension reserves.

Actually, two plans will have substantial numbers eligible for retirement 10 years after the adoption date. At Company B, approximately 10 percent of the current membership group will become eligible for retirement in 1952. A similar proportion, at Company A, will become eligible to retire in 1953. Since the other two firms have only small numbers of employees in the older ages, substantial retirements are not expected for several years.

Severance payments have been the major benefit provided, thus far, by these four firms. Table 4 (page 38) shows that in one case, Company B, approximately one fourth of the total membership group have withdrawn from service with vested rights. In the other three firms less than one half of the withdrawing group qualified for severance benefits, and in one of the three cases, Company C, only one out of every seven qualified.

In some cases death payments have been substantial. All four plans provide this coverage. Since the probability of mortality increases with age, Companies A and B, both with a relatively high average membership age, have paid more in the way of death benefits than either Companies C and D, both of which have a lower average membership age. In one case, Company A, over a six and one-half year period as much as 9 percent of the total membership group were deceased.

Economic conditions and stability of membership groups. General economic conditions exercised some influence upon the stability of pension plan membership groups. Table 5 shows that four firms experienced large withdrawals in the postwar reconversion period (1946–1947).

Table 5. **Average Annual Withdrawal Rate* for Companies A, B, C, and D — 1950**

Year	Company			
	A	*B*	*C*	*D*
1943		1.7%	NA	4.8%
1944	7.8%	0.9	NA	9.5
1945	1.6	2.6	NA	15.5
1946	7.8	8.8	NA	30.9
1947	6.3	3.5	NA	13.1
1948	1.6	12.3	NA	1.2
1949	1.6	6.1	NA	11.9
Average	4.4	5.1	10.4%	12.4

*The withdrawal rate was obtained by dividing the number of withdrawals during the year by the average number of members. (Since average membership data, by years, was not available, the 1949 information was used.)

Transitional re-employment, as well as the withdrawal of females and older employees from the labor force, explain postwar withdrawals. The relatively high rate of withdrawals in 1946, at Company D, suggests that general economic forces affect individual firms in varying degrees.

CHAPTER VI

ADMINISTRATION OF PENSION PLANS

Some aspects of the administration of nine of the pension plans in this study are considered in this chapter. Since pension plan provisions in more than two thirds of them have been amended, this aspect is also considered. Finally, views of employers and pension plan administrators concerning employee interest in the plans are reported and analyzed.

The discussion is limited to the nine voluntary plans; the two union-negotiated plans were not yet in operation as of June 1950. Particular emphasis is given to those seven firms that adopted plans in the period 1941–1943 because they have had an opportunity to develop administrative experience. The seven firms, in the main, employ relatively small numbers of personnel, and in only one case does the work force exceed 200 employees.

Administration

Administrative practices and procedures, such as policy interpretations, record keeping, investment of pension funds, and payment of benefits varied among the plans studied depending upon the method of funding, size of the employer's work force, and particular wishes of employers.

Particular aspects of pension plan administration considered here include administrative practices, procedures, and problems; administrative costs; and administrative review.

Administrative procedures and some problems. Primarily to relieve company personnel of administrative detail, Companies A, B, and H use an outside agency for pension plan administration. They believed that with a professional consultant guiding the administration, there would be less possibility of administrative rulings of the pension committee that are counter to Bureau of Internal Revenue standards. On the other hand, firms that performed their own administration believed, with two exceptions, that detail involved in pension plan administration is not excessive, that personnel in the company can satisfactorily handle the job, and that outside experts may be retained, as needed, on a fee basis. The exceptions were Companies C and D, both of which use individual annuities.

Except for two common problems, both concerned with the administrative detail involved with the preparation of withdrawal notices and the periodic recomputation of benefit levels, employers indicated that there were few administrative difficulties.

Administrative detail involved with pension plan withdrawals, particularly where individual annuity contracts are involved, has proved burdensome in several cases. Moreover, where a pension consultant is retained, a certain amount of duplication of effort is involved, particularly with the pension consultant and the trustee.

Detail connected with the performance of salary reviews is a constant source of irritation to plan administrators, particularly in periods of wage change. Five firms, all employers of small numbers of personnel and using individual annuities, have this problem.[1] At Company D, for example, one employee had five policies, indicating that his benefit level was changed (increased) five times within an eight-year period. Moreover, since trustee charges depend upon the number of policies, administrative costs also increase.[2]

Although an interruption in service beyond the employee's control, such as sickness, does not usually incur a break in pension service, in one plan, Company E, the period of allowable break is not specified but is discretionary with the pension committee. Absence of fixed standards puts broad powers within the control of the employer. On the other hand, where fixed standards are in existence, as in the case of Company A, literal interpretations of the rules are not always made. For example, one employee's sickness has extended beyond the period allowed under the plan, yet the company has continued his policy in force.

Administrative costs. In the nine cases studied, when the plan was adopted, the additional pension duties did not appear to require additional staff. Personnel such as controllers, personnel directors, and factory managers were given the additional duties. Occasionally, duties involved in pension plan administration involve a substantial amount of executive time. For example, three high executives of Company K, who form the investment subcommittee of the pension committee of

[1]In all five cases, benefits are a stated percentage of wages. If wages increase or decrease beyond a certain point, usually enough to effect a $10 change in total benefits, the rate at which pension reserves are accumulated is also adjusted. Wage or salary reviews are performed on an annual or a biannual basis. Since the last decade has been one of rising wage levels, the five firms reported extensive experience with the purchase of additional benefits. In one case, Company B, over 10 percent of the total premium outlay, in 1949, was for the purchase of additional benefits for members.

[2]At Company D the original contract between the company and the trustee provided that the trustee be paid $5 for each contract which was at any time during the year subject to the terms of the trust. The minimum annual fee was $300. As a result of the rising wage level from 1945 to 1949, a large number of additional policies were written. Trustee costs mounted. Taking account of the rate at which additional policies were being written, as well as the lack of precedent for stating trustee charges when the original trust agreement was drawn, the formula for the reimbursement of the trustee was revised: A minimum charge of $5 is made for each participant under the plan. The participant may have up to three policies. An additional charge of $1 per policy is made for each policy in excess of three. The difference in cost among the two methods is significant. For example, under the original agreement a participant with five policies would incur an annual trustee charge of $25. However, under the revised arrangement, the charge is $5.

the plan, require from four to six meetings monthly in order to transact the business of the plan. Usually, however, time spent by company personnel with pension plan administration is not a significant cost item. Heavier administrative costs are incurred by fixed fees, such as trustee fees, pension consultant fees, and brokerage charges. Some plans do not charge the pension fund with such costs. These costs are paid separately by the corporation. For example, the self-administered plan only charges brokerage fees against the pension fund; the actuary's fee and the trustee's fee are paid by the corporation.

Administrative cost experience of only one plan was obtained. At Company A, administrative costs for the year 1949, including primarily pension consultant's fee and trustee's fee, represented approximately an 8 percent additional cost above annual premium payments, and was .005 percent of covered payroll.

Administrative review. Except for the larger firms, such as those with the self-administered trusteed plan and the group annuity plan, there was little incentive to analyze pension experience. Several of the firms studied here employ small numbers of personnel, and, moreover, since they restrict coverage, the actual numbers affected by the plan are very small. Use of a pension consultant, as in three cases, shifts the responsibility for interpretation and analysis of the plan to an outside agency. Finally, in small firms, pension plan administration is a relatively small task for the person usually responsible for plan administration; other larger tasks command more attention.

Pension plan administrators are, in some cases, unfamiliar with their plans. At Company A, the administrator indicated that he was not familiar with the fine points of the plan. Others, such as the administrator of Company C, had little knowledge of the background and history of the company's plan. Cost involved in performing administrative review deters some employers. For example, Company H's treasurer remarked that data on employee benefit plans was "nice to know" but management incurred an expense in collecting, preparing, and analyzing such information. He stated further that in the collection of such data certain liaison work with other departments tended to disturb the normal flow of work.

Pension Plan Amendments and Proposed Changes

In all cases for which information was available (eight voluntary plans),[3] revisions in the original design of the plan were made in order

[3]No information was obtained from Company J, the group annuity plan.

to qualify pension contributions for federal tax deductions. Those revisions were extensive in the case of seven plans adopted in the 1941–1943 period and particularly so with the six firms that employed less than 200 employees. The first amendment of the pension plan of Company H (Appendix B, page 54) is illustrative of the scope of plan revisions made in that period. At least one of the two plans adopted in the postwar period required revision in order to obtain Bureau of Internal Revenue approval, but the changes were only minor.

Only four of eight firms indicated satisfaction with the current design of their plans. However, Company G's plan was only adopted in 1947, and Companies H and K have revised their original plan. Actually, in only one case, Company C, was there general satisfaction with the plan as initially constructed. Four other firms voiced dissatisfaction with the current design of their plans. Employer representatives, in each case, indicated the precise nature of the plans' failings, the proposed change, and listed the specific problems connected with making changes.

Company A's president stated that the vesting provision, which grants vesting after only five years of service, was too liberal. He was considering amending the provision, but for two reasons has neglected to take any action. On the one hand, there have been only few vested withdrawals; on the other, since the company is not unionized, any modification in the design of the plan would tend to undermine the employee's confidence in the management. Moreover, according to the pension consultant, the benefit formula has proved inadequate. Although, by granting credit for past service, this firm intended to treat favorably older long-service employees, subsequent operation of the plan has proved otherwise. Actually, the benefit formula results in proportionately smaller benefits for the senior worker and proportionately larger benefits to the younger employee.

According to Company B's treasurer, the absence of a minimum age rule for participation is a major deficiency of the plan. A minimum age qualification, at say age 35, would eliminate the expense involved in the payment of vested benefits to youthful male and female withdrawals. Here, the inability of the management to "sell" the workers on such a change, prevented the easy adoption of such an amendment.

Company D's controller indicated that both the service requirement for eligibility to participate and the vesting provision should be revised in order to control pension costs more adequately. To eliminate the cost involved in the payment of withdrawal benefits, particularly to short-service male employees, he proposed that the service requirement for participation be increased from two years to five years, and that vesting be on a graduated scale based on service, rather than immediate vesting after two years of membership. Difficulties involved in the processing of amendments, particularly with reference to the Bureau of Internal Revenue, according to this employer, and the inability to gauge the effect of pension plan changes on the labor relations of the company, prevented immediate revision.

Company E's president, who at the time of this study was carrying on discussions with advisors preparatory to amending the pension plan, claimed that extensive revisions of his plan were imminent. Proposed changes of some importance included the lowering of the service requirement for participation from five years to three years in order to make the plan applicable to a larger portion of the work force, as well as the reduction of the benefit level from 60 percent of wages to 40 percent of wages, a level more in keeping with Company E's current ability to pay. This employer, whose total work force did not exceed 30 employees, was independently revising his plan. Discussions with insurance agents and other employers, and a study of other plans, were helpful, he stated, in formulating changes.

Shortcomings in the original design of pension plans, particularly those adopted in the 1941–1943 period by small firms, are explained on several grounds. Generally, there was a lack of knowledge and experience concerning pension plans. Certainly, few employers were schooled in pension plans. Evidence suggests, moreover, that, at that time, the employer's advisors, customarily insurance agents, were not experienced with the design of pension plans. Two pension consultants, servicing three firms, indicated that such was the case. One remarked, "At that time, the level of knowledge of pension plans, even among consultants, was not high." Company B's treasurer indicated that the management, in 1942, attempted to obtain experience of pension plans as a guide in the design of its plan but found none.

Pension planners also had difficulty interpreting the federal statute affecting pension plans. Since the federal regulations were revised in 1942, in the 1941–1943 period new regulations were being contemplated or had been only recently enacted. The seven plans studied here and adopted in that period were, in a sense, experimental because few knew what would "go" with the Bureau of Internal Revenue. The pension consultant servicing the pension plan of Company H indicated that the 36 percent benefit level of the plan is explained, in part, on that basis. Likewise, at Company A, the pension consultant stated that something in the way of full immediate vesting was visualized as necessary for obtaining Bureau approval.

Changing employment patterns promoted changes in pension patterns. Occasionally, as in the case of Company B, eligibility rules were based on prewar patterns of employment which were not duplicated in the postwar period. In other cases, as in the case of Company D, the quality of turnover data was questionable. However, as noted previously, even where accurate data were used, withdrawals have exceeded estimates.

Finally, in several cases, the adoption of the pension plan was generally a one-man job. This was particularly true in the case of the small firm, such as Companies A, E, and H. No attempt was made to solicit the opinions of officers of the company involved concerning the merits of the plan. In one case, Company E, the immediate personal gain of one company official appeared to be the chief motive for the plan's adoption.

Employer Views on Employee Interest in Pension Plans

Lack of employee interest in the plan, according to pension plan administrators and employers, suggests that some of the immediate advantages expected from the plan, such as improved morale and enhanced efficiency, have not been realized. The following comments illustrate employer views. Company A's president stated that surprisingly few questions or explanations concerning the plan are requested by employees. "Very few of the permanent employees make inquiries," he remarked. Company B's treasurer stated that younger employees, particularly female employees, are uninterested in the plan. According to Company D's controller, employee response to the pension plan has been "cool." Company E's president remarked, "The worker is unaware of what the company is doing for him in the way of pensions." This employer believed that wages were the employee's major concern. In order to increase interest in the plan, employers were considering several remedial measures.

Employers with noncontributory plans, such as Companies A and B, believed that employee interest would be enhanced if their plans were contributory. But employers with contributory plans, as in the case of Company C, also have similar problems with maintenance of employee interest. Moreover, attempts to increase interest by sending employees annual statements of their pension account, as in the case of Companies A and B, appear to have had little positive effect.

Lack of employee interest in pension plans may be attributed to several factors.

1. Nearly all voluntary plans were employer-initiated and are employer-administered. Since employees normally played little part in the adoption of the plans and have no say in administration, they have had no opportunity to develop an interest in the plan.
2. Large numbers of an employer's work force (see Table 2, page 12) normally do not participate in the plan.
3. Voluntary pension plans are noncontractual and may be discontinued at any time, although Bureau of Internal Revenue regulations place certain restrictions on easy termination. (The fact that in the event of termination the proceeds of the trust would become the property of the members was perhaps not common knowledge to members. In all probability, some members believed that employers could recapture pension contributions.)
4. Except for one firm that granted full immediate vesting, a majority of the members who severed employment received no benefits, thus tending to undermine the employee's confidence in the plan.
5. In some cases, pensioners have received small benefits; in others, few or none have been retired.

Employer techniques for publicizing their plans in order to create employee interest in the plan are of uneven quality and, in some cases, entirely neglected. The initial oral explanation of the plan to new members in several cases was very brief. The purchase of additional benefits, a regular procedure in the case of six individual annuity plans, was "routine" according to several employers. Three firms, Companies A, E, and G, gave members no descriptive literature; the pension trust agreement retained in the employer's files was the only descriptive document of the plan. Six other plans issued descriptive literature; however, in three cases, a copy of the trust agreement was issued. Thus, in only three voluntary plans are members given descriptive material which may be readily understood.

CHAPTER VII

CONCLUSIONS

The pension plans of the eleven Western New York firms included in this study were adopted during 1941–1950, a period generally favorable to that kind of innovation in employer-employee relations. During the first half of the period, increased taxation, wage and salary stabilization policies, and scarcity of labor were crucial problems for which pensions seemed to offer some solution. Although the importance of these factors varied, a majority of the firms introduced pensions hoping thereby to increase worker efficiency, lower turnover, and attract skilled and experienced personnel. The retirement of superannuated employees and an improvement in the community and employee relations also were incentives for introducing employee pensions. The two employers who set up collectively bargained pension plans in 1950 also expected gains in increased community and employee good will with the other advantages playing a less persuasive role.

Conclusions based on analysis of the provisions and operating experience of these eleven plans must, of course, be tentative. The diversity among both the companies and plans in this sample, however, suggests that the following six conclusions may have wider application:

1. Few of these employers have realized the immediate advantages expected from their pension plans. There is no evidence, for example, that employee separations were substantially reduced (Chapter V). Separations were sometimes unexpectedly large among the experienced male employees. For example, in at least four plans the average age of withdrawing employees ranged from 36–40, a period often believed to constitute the worker's most productive years. Some firms failed to retire their employees at normal or "plan" retirement age (Chapter III). This suggests that, to date, at least, their plans have not been effective in accomplishing "orderly" or "uniform" retirement. Employer reluctance to implement compulsory retirement implies also that employee superannuation bears little relationship to the plan retirement age. Indeed, the two concepts may be mutually contradictory. Finally, while certain tax advantages have been realized, pension costs have constantly increased as wage levels have climbed. This increased cost of benefits has reduced or offset the attractiveness of the tax reduction feature.

2. Analysis of the coverage and withdrawal experience of these plans does not support a widely held opinion that private pension plans restrict labor mobility.[1] The coverage provided limits any restrictive influence to that portion of the work force least likely to change jobs and which has a strong attachment to a single employer for other reasons. The findings of at least one recent labor market study[2] are consistent with this conclusion. The composition of the withdrawals experienced by all but one of the firms for which information was available, on the other hand, indicates that labor mobility has not been markedly changed by the introduction of the plans. In most of these instances, younger workers and female employees marginal to the firm's labor supply made up the bulk of the separations. In the case of the older worker, on the other hand, the provisions of most of these plans, because of the increased cost of providing retirement benefits, only intensify existing practices that already restrict the range of his employment opportunities.

3. An analysis of the findings with respect to coverage, membership, and vesting suggests, furthermore, that only for a relatively small group of employees is there a prospect of a retirement income from these plans. The two union-negotiated plans excepted, about 50 percent of the employees were not covered by the plans; two covered only salaried employees (Chapter II). Minimum age requirements, ranging from 25 to 30, and service requirements of as much as five years in three plans, on the one hand, and maximum age requirements for initial plan coverage, on the other, together set narrow limits for employee participation (Chapter II). Service requirements for vesting, superimposed on the service required for plan participation, further reduce the benefit rights of employees whose permanency of tenure is not well established. As a result of these requirements, the potential beneficiaries of most of these plans are a group of permanent employees for whom employers are willing to invest the amount required for benefits at retirement age. Such an employee is usually between the ages of 30 to 50, male, probably skilled or salaried, and with a work-life expectancy of 15–30 years.

From the standpoint of the individual worker the coverage under private plans is not as dismally poor as is here implied. The fact that worker A did not stay with employer X long enough to qualify does not exclude him from private plans indefinitely. He may become permanently attached to employer Y with his very next job. We must not

[1]Sumner H. Slichter, "The Pressing Problem of Old-Age Security," *New York Times Magazine*, Oct. 16, 1949, p. 66; and Clark Kerr, "The Social and Economic Implications of Private Pension Plans," *Reprint No. 16*, Institute of Industrial Relations, Berkeley, Cal., 1949, p. 5.

[2]Lloyd G. Reynolds, *The Structure of Labor Markets*. New York: Harper's, 1951, p. 80.

forget that the identity of the individuals in the group of uncovered workers is constantly changing.

Nevertheless, competent observers of pension practices have held that the limited number of plans now in existence and the increasing tendency to establish maximum age for participation (through service requirements) make it doubtful that employees who do move from job to job will acquire sufficient service with one employer to qualify for a pension. The experience of the companies in this study does not justify any other conclusion.

4. Although the experience of these plans is limited, it leads to the conclusion that retirement security for many employees is not easily attained. This is particularly true in the case of the newly hired older worker, since he has no prior accumulation of pension credits. Occasionally, such workers are excluded from participation (Table 2, page 12). His situation is acute in the event that disability or other considerations force his retirement before other sources of income, particularly OASI benefits, are available.

5. Minimal, or at least modest, benefits have been provided for most of the employees who have retired under four of these plans. Of the ten employees who retired from one company, in 1949, three received average monthly benefits of $33 exclusive of OASI; the benefits for which seven others were eligible were so low that the company substituted lump-sum payments, ranging from $25 to $1,100.

The absence of minimum benefits adjusted to current planes of living, the benefit formulae, and the provisions for vesting further reduce the importance of these plans as retirement security devices. In at least seven of the plans studied the benefit formulae favored employees at the top of the wage and salary structure. In five plans, the flat percentage of compensation formula severs the relationship between wages and benefits five years before retirement although, as recent experience shows, significant changes in the cost of living may occur over much shorter periods. The variety of vesting options provided by more than half of these plans, particularly the individual annuity plans, further weakens their effectiveness. This is particularly marked in cases where accrued annuity values are readily convertible to cash. When, in such cases, many employees surrender paid-up deferred annuities, it is difficult to escape the conclusion that the plans function not as pension or retirement devices, but rather as private savings or deferred compensation programs.

6. Limited coverage of the work forces, nonvested withdrawals, low benefits, and, in a majority of the cases, integration of plan benefits

with OASI indicate that, for most employees, the main reliance for retirement income must be placed on governmental programs. The fact that the employers in five of the seven companies integrating pension plan and OASI benefits expected to reduce their plan contributions instead of increasing the total benefits (Chapter IV) highlights that observation. The dominant role of OASI becomes even more obvious where large groups of employees remain outside the coverage of the private plan. Even in union-negotiated plans where coverage is universal, the 15-year service requirement for benefits means that many employees will never qualify for benefits.

7. Although differences in pension problems among the firms studied were usually one of degree, occasionally distinctive problems appeared, which were attributable to the size of the work force and the financial flexibility of the firm. The fact that some unions, such as the United Steelworkers of America, CIO, have made little or no attempt to obtain pensions from small firms is evidence that unique problems are involved.[3]

Funding methods available for small organizations are limited and very costly. Size of the work force alone normally precludes the use of a self-administered trusteed plan and a group annuity plan. Certain employers may be opposed to profit-sharing retirement plans. Thus, the only readily available alternative[4] for the small firm is relatively high cost coverage through individual annuity policies.

Since the major concern of employers in the firms here studied was ability to pay for pensions, particularly over a period of years, the experiences of two small firms offer guide lines in that connection. Both use the money-purchase benefit formula. At Company A, pension contributions remain at approximately 5 percent of covered payroll after six years of experience. Company G's profit-sharing retirement plan provides optimum funding flexibility because no contributions are required when there are no earnings.

---

[3]In one region, District 4, United Steelworkers of America, CIO, a careful check of the union's publication, *The District Observer*, showed that, in a period when numerous pension agreements were negotiated, not one small organization signed a pension agreement: From Jan. 1, 1950 to July 1, 1950 contracts were negotiated by 12 firms, all employing less than 200, but only wage increases and group life, hospitalization, surgical, and nonoccupational disability benefits were granted.

The probability of exposing the small firm to financial insecurity, thereby jeopardizing the job security of the union members, on the one hand, and lack of sufficient profit margin to provide the unions' minimum standard benefit, on the other, explain the absence of pensions among small firms. Furthermore, the union leadership found little support for pensions (to the extent that members would strike in support of pensions), even though, in some cases, large numbers of senior workers were involved.

By stimulating the enactment of the Social Security Act Amendments of 1950, the general pension "drive" of several large industrial unions was of some significance to all workers covered by OASI.

[4]Deposit Administration, as well as area plans, such as the "Toledo Plan" offer some solution today.

Small firms normally devote little time to the administration of the plan and, in some cases, retain an outside agency to administer the plan. Insufficient regard to administration allows abuses to go unchecked; furthermore, there is little incentive to analyze experience with an intent to improve the plan.[5]

[5]An outstanding exception, however, is Company H (see Appendix B) where frequent changes in the plan are made.

APPENDIX A

Participating Companies and the Nature of Their Pension Plans, 1950

PARTICIPATING COMPANIES				NATURE OF PENSION PLAN					ELIGIBILITY RULES FOR PARTICIPATION	
Company	Number of Employees	Type of Company	Unionization (Hourly Paid Employees)	Method of Adoption	Funding Method	Contributory or Noncontributory	Date Adopted	Definition of Coverage	Age Requirements	Service Requirement
A	90	Manufacturer of screw machine products	No Union	Voluntary	Individual Annuity	Noncontributory	July 1943	All Employees	Over Age 25 Under Age 55	3 years
B	190	Wholesale distributor of industrial supplies and steel	Unionized	Voluntary	Individual Annuity	Noncontributory	December 1942	All Employees	Under Age 65	3 years, 11 months
C	90	Wholesale distributor of industrial supplies	No Union	Voluntary	Individual Annuity	Contributory	May 1942	All Employees	Under Age 60	4 years
D	160	Manufacturer of metal punching and notching equipment	Unionized	Voluntary	Individual Annuity	Noncontributory	December 1942	All Employees	Under Age 70	Hourly pd.—2 yrs. Salaried—1 yr.
E	30	Manufacturer of metal gears	No Union	Voluntary	Individual Annuity	Noncontributory	November 1941	All Employees	Under Age 55	5 years
F	400	Manufacturer of steel bars and shapes (re-rolling mill)	Unionized	Collective Bargaining	NA	Noncontributory	March 1950	All Employees	None	None
G	100	Wholesale distributor of millwork	Unionized	Voluntary	Profit-Sharing	Noncontributory	1947	Salaried Employees Only	Under Age 60	5 years
H	200	Manufacturer of crucibles, refractories, highspeed grinding wheels, etc.	Unionized	Voluntary	Individual Annuity	Contributory	October 1941	Salaried Employees Only	Over Age 25 Under Age 60	1 year
I	9,000	Manufacturer of gas and diesel engines, air and gas compressors, etc.	Unionized	Collective Bargaining	NA	Noncontributory	July 1950	All Employees	None	None
J	750	Manufacturer of adding machines	Unionized	Voluntary	Group Annuity	Contributory	May 1948	All Employees	Over Age 30 Under Age 65	5 years
K	4,000	Purchaser and seller of farm equipment and farm supplies	Partly Unionized	Voluntary	Self-Administered Plan	Noncontributory	July 1943	All Employees	Over Age 25 Under Age 53	3 years

APPENDIX B

Amendments of Pension Plan of Company H

Effective October 15, 1941, Company H adopted a contributory pension plan for salaried employees. In the following eight years, the plan was amended six times. The main features of the amendments are summarized below.

First Amendment: Effective October 15, 1943.

Eligibility rules and the method of joining the plan were spelled out in detail. Service under the plan was defined, particularly with regard to leave of absence and military leave. The benefit level was reduced from 36 percent of wages to 30 percent. The "10-year certain contract" became the standard policy purchased. Salary was carefully defined, including the basis for determining earnings for personnel paid on a part-salary basis and part-commission basis. Certain restrictions connected with the increase of benefits, including the method of making such changes, were listed. The vesting provision was spelled out in detail including the disposition of contracts in the event of routine withdrawal, death or leave, retirement on leave, and failure to return after termination of leave, particularly military leave. One of the trustees of the plan was changed. Since the amendment included a statement indicating that all affected employees had read the agreement, their signatures were on the amended plan.

Second Amendment: Made October 13, 1944, retroactive to October 15, 1943.

Employees who failed to join the plan when they first became eligible were required to join within three years of that date, otherwise the right to participation was forfeited. Contracts purchased for members were to contain, as far as possible, like or similar basic options, and cash surrender values. Amounts borrowed on a specific contract, in order to meet premium payments, were applied only to the premium payment on that specific contract. Employer contributions, recaptured in the event of withdrawal of a member, were left in the trust and applied toward the payment of current premiums. In the event of discharge for cause, the withdrawing member was ineligible for vested rights. Leaves of absence, other than military leaves, were limited to 18 months.

Third Amendment: Effective October 3, 1945.

Eligibility rules, salary, and continuous service were further defined. Employees who failed to exercise rights under the plan were required to do so within three years after the right accrues, otherwise a "new" period of service was required. Disability retirements were allowed to rejoin the plan immediately upon reinstatement to service. Reductions in salary were to be in effect for two consecutive anniversary dates before plan benefits were reduced. Employees were notified in the event of reduction in benefits.

Fourth Amendment: Effective October 15, 1947.

Since the pension trust agreement had been extensively revised up to this point, in order to facilitate the administration of the plan, the fourth amendment restated the entire trust agreement. Moreover, for easy reference, the entire plan was indexed.

The fourth amendment made several important changes. Discharge for cause was defined. Service was further defined. A suspense account was created as a depository for nonallocated funds. A "spendthrift" clause was put in effect. The benefit level was raised to 36 percent of wages. The procedures and rights, in the event of either company or employee default in premium payment, were spelled out in detail.

Fifth Amendment: Effective October 15, 1948.

The vesting provision was revised.

Sixth Amendment: Effective October 15, 1949.

For all members, rather than deduct the members' expected Federal Social Security benefit from the total benefit provided by the plan, an arbitrary sum of $50 was deductible. That change introduced a fixed deduction from total plan benefits, thus easing the administrative burden of the plan. Moreover, since the modification was made with the expectation that Federal Social Security benefits would be liberalized, plan members would also profit by the change.

APPENDIX C

General Classification of Pension Plans by Funding Procedures

FUNDED (QUALIFIED PLANS UNDER 165 (a))

Insured: Individual Contract Plans (Trustee Required)	Insured: Regular Group Annuity	Insured: Deposit Administration Group Annuity	Self-Administered
Individual insurance contracts plus or minus life insurance.	Individual benefits bought, and money allocated currently as received.	Fund is not allocated.	Fund is not allocated. Invested by the Trustee in conservative securities.
Level premium. Rates include cost for death benefit in the form of life insurance or lump sum equal to total premiums.	Single Premium Deferred Annuity. Generally step-rate calculations.	Life annuities bought from fund at insurance company rates as each employee retires.	Pension benefits paid from the fund.
No discount for turnover.	Premiums at rates determined by insurance company. (Guaranteed 5 yrs.)	Actuarially determined cost on step-rate or level basis. Frequent valuations	Actuarially determined cost on step-rate or level basis.
	Company cost discounted for deaths. No discount for turnover.	Assumptions of interest, mortality, and turnover made on conservatively realistic basis.	Assumptions of interest, mortality, and turnover made on conservatively realistic basis.

PARTIALLY FUNDED (THROUGH A TRUSTEE)

During Employment	At Retirement
Current service paid and only interest on past service.	Single amount, calculated to be sufficient to pay the life income, contributed to fund at time employee retires. Modification: Pay this single amount in five annual installments plus interest starting at employee's retirement.
Actuarially determined future cost on step-rate or level basis.	Procedure to meet term of agreement under labor contract.
Assumptions of interest, mortality, and turnover made on conservatively realistic basis.	

Will not qualify under 165(a) until the Bureau of Internal Revenue modifies its thinking which may be soon.

UNFUNDED (PAY-AS-YOU-GO)

Discretionary	Uniform by Formula	
No formula.	Book reserve or pay out of current company income.	Book reserve or pay out of current company income.
Benefits based on need, generosity of management or personal liking.	Plan announced.	Plan not announced.

Low cost at start—costs pyramid later.

Compiled by G. Gilson Terriberry Company, New York City.

APPENDIX D

Glossary of Terms

Usual Meaning as Applied to Pension Plans

Compiled by G. Gilson Terriberry Company, New York City

Pension Plan — A formalized program for determining the lifetime incomes to be paid to employees after retirement.

Funded — Cost of ultimate benefits actuarially determined and reserves established during employees' working years.

Partially Funded — Actuarial reserves not fully established during employees' working years.

Unfunded (Pay-As-You-Go) — Meeting pension costs only as actual payments are made to pensioners — No advance funding of any kind.

Insured Plan — A plan funded through an insurance company.

(a) Group Annuity Plan — Annuities purchased for each individual as premiums are paid under group contract.

(b) Deposit Administration Plan — Contributions are paid under a group contract and are accumulated with interest in an unallocated fund from which is drawn at retirement an amount sufficient to purchase a single premium annuity.

(c) Individual Contract Plan — Contributions are used to purchase for each individual a retirement income contract which may or may not include life insurance.

Self-Administered (Trusteed) Plan — Plan funded through a trustee who may be a bank, an individual or group of individuals. Each year an actuarially determined amount is paid to trustee. Pension payments will be made from the fund as they fall due.

Profit-Sharing Pension Plan — Percentage of profits distributed equitably by formula to account of each employee. Accumulated amounts used to purchase pension. Thus the amount of contributions determines the pension.

Contributory — Employee and employer both share in the cost.

Noncontributory — Employer stands entire cost.

Unit Purchase Plan — Formula of pension benefit is fixed and the cost varies.

Money-Purchase Plan — Formula of contributions is fixed and the amount of pension varies.

Final Pay Plan — Amount of pension based on earnings just prior to retirement or the average earnings for a short period of years just prior to retirement. May include proportionate reduction for shorter service.

Average Pay Plan – Amount of pension based on earnings during credited years. Includes plan where benefit is a percentage of each year's earnings.

Flat Benefit Plan – Plan provides uniform pension regardless of earnings. Usually specifies minimum service requirement with proportional reduction for shorter service. Benefits from Social Security often taken as an offset.

Mortality Table – A table showing how many individuals, starting at a certain age, will be alive at each succeeding age. Used to give the probability of dying in, or surviving through, any period. Based on experience of individuals with something in common such as sex, occupational group, calendar years, etc.

Mortality Table Rated Back (Modified) – Using the mortality and life expectancy rates for a younger age than that shown in the basic table, thus producing a new table.

Example: 1st Modification – Age 63 uses age 62 rates, age 30 uses age 29 rates, etc.

Life Expectancy – Average number of years of survival for a group of individuals after a given age.

Discounts for Deaths – Decrease in costs resulting from assumed incidence of deaths both before and after retirement.

Actuary – A person skilled in the science of applying the probabilities of longevity to financial and other operations. Recognized professional standing is obtained through membership by examination in the Society of Actuaries, first as an Associate and later as a Fellow.

Actuarial Equivalent – A rate of pension of equal value to another after giving consideration to altered incidence of mortality and interest caused by optional age or form of pension.

Actuarial Reserve – Present value of future pension payments which are contingent upon the death or survivorship of one or more individuals. It is computed on assumptions that interest will be earned at a specified rate and mortality rates and other changes will follow a specified schedule.

Turnover Rates – Rates at which employees terminate service for reasons other than death – must know variations by age, service, and sex to be usable for pension cost computations.

Termination Credits – The funds released for reallocation when an employee's service with the company ends and he does not retain a right to receive a pension. Does not apply to the extent costs had already been reduced by expected turnover.

Future (Current) Service Benefits — Retirement credits accruing during the period of membership in the pension plan — that is, after its installation and prior to retirement.

Past (Prior) Service Benefits — Retirement credits for service prior to installation of plan.

Minimum Benefits — A basic pension which will be provided if standard formula should produce less. Benefits from Social Security often taken as an offset.

Supplemental Payments — Payments made out of pocket to retired employees in addition to benefits from pension plan.

Vesting — Attainment of a right to a deferred pension without the necessity of continuing employment.

Permanent and Total Disability Benefit — Incomes for employees who become physically unable to continue work but are not old enough to retire.

Future (Current) Service Cost — Actuarially determined amount to fund future service benefits.

Step-Rate Funding — Funding each year the cost of that year's credited pension. Cost per individual normally increases each year.

Level Premium Funding — Funding part or all of the pension costs by equal payments during each employee's working years under a retirement plan. It may be level in dollars or a level percentage of employee's earnings.

Past Service Liability — Amount actuarially determined at start of plan to fund costs of past service benefits.

Past Service Funding — Paying cost of past service liability; may be paid all at once or amortized over period of years. Minimum aggregate payments at any time must be equal to interest on original liability. Maximum amount that may be used as tax deduction in any one year is 10 percent of original liability.

Qualified Plan — A formal, funded, nondiscriminatory pension plan approved by Bureau of Internal Revenue (has tax advantages to employer and employee). Section under which it qualifies is 165 (a) of the Code.

Nonqualified Plan — Not approved or not approvable by Bureau of Internal Revenue (usually is disadvantageous tax-wise).

Mimeograph 5717 — A release of the Bureau of Internal Revenue which describes:

(a) Cut-back of benefits to certain high paid employees if plan terminates within the first 10 years.

(b) Minimum rate of funding below which Treasury Department will deem plan to be terminated.

Deduction under 23 (p) – Refers to Section of Bureau of Internal Revenue Code under which costs of qualified plans are claimed as business expense.

Social Security Integration – Testing of combined pensions provided by Social Security plus pension plan. Total shall not be proportionately greater for higher salaried employees than for lower paid employees.

Normal Retirement Date – Date established by plan for regular retirement.

Early Retirement Date – Date prior to normal retirement when employee may retire.

Deferred Retirement Date – Any retirement date after normal retirement date.

Retirement Annuity – General term for annual income payable at retirement for life.

Life Annuity – An annual income starting at retirement and continuing for life with no further payment of any kind after death.

Modified Cash Refund Annuity – Annual income starting at retirement and continuing for life with guarantee that if employee dies before receiving in pension an amount equal to his own contributions and interest, any balance will be paid to his beneficiary.

Cash Refund Annuity – An annual income starting at retirement and continuing for life with guarantee that if employee dies before receiving in pension the total value of annuity at retirement date, any balance will be paid to his beneficiary.

10 Years Certain and Life Annuity – An annual income starting at retirement and continuing for life with guarantee that if employee dies within 10 years after retirement, payments will continue to his beneficiary for balance of the 10 years.

Joint and Survivor Annuity – An annual income starting at retirement and continuing for life with guarantee that if employee dies while his contingent annuitant is living, payments on a predetermined rate will continue to the contingent annuitant for life.

PUBLICATIONS

THE PUBLICATIONS PROGRAM of the New York State School of Industrial and Labor Relations includes the quarterly magazine, *Industrial and Labor Relations Review;* a series of research monographs, CORNELL STUDIES IN INDUSTRIAL AND LABOR RELATIONS; a book series; and a series of bulletins. These bulletins were formerly designated as "Research" or "Extension." Beginning with Bulletin No. 15, the two series of bulletins were combined into one general series.

Persons interested in receiving the "List of Publications" may write to the School and be placed on the mailing list to receive the announcement of publications as it is revised periodically.

PRICES OF PUBLICATIONS

Bulletins are free to New York State residents. Charges as noted are for out-of-state requests and for in-state orders of over five copies.

The *Industrial and Labor Relations Review,* a quarterly magazine, is $4.00 per year by subscription.

CORNELL STUDIES IN INDUSTRIAL AND LABOR RELATIONS, the research monograph series, is distributed with a nominal charge (based on printing and distribution costs) as indicated in the listing of volumes.

Prices of volumes in the INDUSTRIAL AND LABOR RELATIONS BOOK SERIES are listed on the next page.

Bulletins

The following bulletins are currently available:

E 2 *You Can't Hire a Hand, and Other Essays,* by Temple Burling. Extension Bulletin No. 2, February 1950. 30 pp. 10¢.

E 3 *Our State Safety and Health Laws,* by Lois S. Gray. Extension Bulletin No. 3, March 1950. 28 pp. 10¢.

E 4 *Sources of Information on Union-Management Relations,* by J. Gormly Miller. Extension Bulletin No. 4, March 1950. 34 pp. 10¢.

E 5 *Introduction to Public Relations,* by Dave Hyatt. Extension Bulletin No. 5, September 1950 (Reprinted December 1951). 104 pp. 25¢.

E 6 *Out of Work,* by John N. Thurber. Extension Bulletin No. 6, September 1950. 36 pp. 10¢.

E 7 *Improving the Supervision in Retail Stores,* by Paul J. Gordon. Extension Bulletin No. 7, October 1950 (Reprinted March 1952). 64 pp. 15¢.

R 5 *Combating Discrimination in Employment in New York State,* by Felix Rackow. Research Bulletin No. 5, November 1949. 52 pp. 15¢.

R 6 *Negroes in the Work Group,* by Jacob Seidenberg. Research Bulletin No. 6, February 1950 (Reprinted February 1951). 48 pp. 15¢.

R 7 *Seniority Rights for Supervisors?* by Rexford P. Kastner. Research Bulletin No. 7, September 1950. 60 pp. 15¢.

G 15 *Sampling—Elementary Principles,* by Philip J. McCarthy. Bulletin No. 15, March 1951. 34 pp. 25¢.

G 16 *Role-Playing in Action,* by Chris Argyris. Bulletin No. 16, May 1951 (Reprinted April 1952). 30 pp. 15¢.

G 17 *Day In, Day Out with Local 3, IBEW: A Study of Local Union Government and Administration,* by Maurice F. Neufeld. Bulletin No. 17, June 1951. 54 pp. 15¢.

G 18 *Economic Security: A Study of Community Needs and Resources,* by John W. McConnell and Robert Risley. Bulletin No. 18, July 1951. 92 pp. 25¢.

G 19 *Manpower, Wages, and Labor Relations in World War II: An Annotated Bibliography,* compiled by Donald Ghent, Gladys Waltcher, and Edwin Beal, under the direction of J. Gormly Miller. 100 pp. 25¢.

G 20 *Industrial Training: A Guide to Selected Readings,* by John M. Brophy, I. Bradford Shaw, and Fred T. Golub. Bulletin No. 20, May 1952. 72 pp. 25¢.

Periodicals

Industrial and Labor Relations Review. A quarterly magazine issued in January, April, July, and October. Each issue not less than 160 pages. Four dollars ($4.00) per year by subscription.

"Abstracts and Annotations." A monthly digest of selected articles in current and periodical literature on industrial and labor relations. Each issue approximately ten pages. Mimeographed. Free.

Cornell Studies in Industrial and Labor Relations

Wartime Manpower Mobilization: A Study of World War II Experience in the Buffalo-Niagara Area, by Leonard P. Adams. Volume I. $1.00.

AFL Attitudes toward Production: 1900–1932, by Jean Trepp McKelvey. Volume II. $1.00.

Industrial and Labor Relations Book Series

A series of books dealing with industrial and labor relations, sponsored by the New York State School of Industrial and Labor Relations, and published by the Cornell University Press. (May be purchased at your bookstore or from the Cornell University Press, 124 Roberts Place, Ithaca, New York.)

Employers' Associations and Collective Bargaining in New York City, by Jesse Thomas Carpenter. 437 pp. $4.50.

Heritage of Conflict: Labor Relations in the Nonferrous Metals Industry up to 1930, by Vernon H. Jensen. 508 pp. $4.75.

1

W. F. HUMPHREY PRESS INC.
GENEVA, N. Y.