RECORD OF SOCIETY OF ACTUARIES
1975 VOL. 1 NO. 3

MEETING A POPULATION'S RETIREMENT NEEDS

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1. What are the retirement needs of a population?
2. What are suitable methods of providing social insurance, private pensions, and savings?
3. What are the political, economic, and sociological implications of various solutions?
4. What perspective on this problem does Canadian experience provide?

MR. CLAUDE B. GARCIA: Meeting a population's retirement needs constitutes one of the greatest challenges facing social planners both within and outside government today. This challenge will become even greater in future years due to both the increased proportion of individuals who reach retirement age and the sharp decline in the birth rate.

With the passing of time, a distinction has been established between the retired population and the rest of us. Age 65 has become the traditional age for retirement. It has become very difficult for people aged 65 and over to find remunerative employment. In September 1974, for example, one in ten persons aged 65 or over in Quebec had a job.

For older Canadians, income from work has been replaced by income from pensions, mainly government pensions. The income maintenance system for the older Canadians is based on a combination of the Social dividend and the negative income tax with a seasoning of social insurance. All Canadians aged 65 and over who can satisfy fairly liberal residence requirements are eligible to receive a monthly pension of $123.42 1/, escalated every three months according to increases in the cost of living. This pension paid by the Federal government is subject to income tax but the Federal income tax exemption has been increased by $1,174 in 1975 for all persons aged 65 and over. Because of this additional exemption, approximately 75% of the pension will escape tax altogether.

Any person eligible to receive the old age pension can claim the guaranteed income supplement of $86.57 per month for a single individual and $153.76 per month for a retired couple. The monthly supplement, also escalated every three months, is reduced by $1 for each $24 of annual income(i.e.,50% tax-back)received during the previous calendar year. The supplement is not subject to taxation.

The Canada/Quebec Pension Plan enables the pensioner to retain 25% of the average monthly earnings payable as early as age 65. The yearly maximum pensionable earnings should be increased each year until equal to fifty-two times the average weekly earnings in Canada. This level is not expected to be reached before 1980. Average weekly earnings in Canada stood at $188 in November 1974. The retirement pension is calculated so as to reflect any increase in productivity before retirement. Once paid, the pension is escalated yearly to the full cost of living. The pension is taxable and will reduce the

1/ All figures in Canadian dollars.

guaranteed income supplement at the rate of $1 for each $2 of pension paid 2/.

Private pension plans also play a limited role in assuring financial security for the old. In 1973, Canadians received approximately $900 to $1,000 millions in pension benefits (excluding refunds) 3/. During the same period, the Canada/Quebec pension paid $400 millions in benefits and the Federal government disbursed $3.1 billion for old age security and the guaranteed income supplement. This meant one dollar for each four dollars received from State pension plans.

Whether this situation will change or not in the next few years will depend on the relative rate of growth of the Canada/Quebec Pension Plan and the private pension plans. The Canada/Quebec Pension Plan will pay its first maximum pension in 1976 and will therefore continue to extend its role in providing income for the retired population in the next few years.

Only 39.2% of the labour force participated in private pension plans in 1970 4/. This participation rate falls to 30.7% when employees of the public sector are excluded. This low participation rate is generally explained by the low salaries paid to those excluded 5/.

Table 1

Contributors to a private pension plan by income class in Quebec, 1972 taxation year -

Income classes	Number of persons contributing to a private pension plan	
	As a proportion of all taxpayers	As a proportion of taxpayers who had income from employment
Less than $2,500	4.8%	5.7%
$2,500 to $5,000	13.0	14.7
$5,000 to $7,500	34.0	36.3
$7,500 to $10,000	53.2	55.8
$10,000 to $15,000	59.6	63.2
$15,000 to $20,000	57.3	64.6
$20,000 to $25,000	46.8	57.2
$25,000 to $50,000	33.6	46.1
$50,000 to $100,000	19.8	31.9
$100,000 and more	20.3	32.3
Average	33.7%	36.9%

Source: Ministère du Revenu du Québec, Statistiques fiscales, 1972. Unpublished data.

2/ By exception, the current year retirement pension is used in the calculation of the guaranteed income supplement.

3/ Precise statistics are not available.

4/ Statistics Canada, Pension plans in Canada, cat. 74-401 table B.

5/ A worker whose average earnings would be slightly lower than the yearly maximum pensionable earnings will draw from the government a pension equal to more than 40% of his previous earnings.

However, according to Table 1, this explanation is not quite sufficient. In 1972, 36.3% of salaried workers whose total income stood between $5,000 and $7,500 admitted participation in contributory private pension plans. This proportion stood at 55.8% for workers with total income between $7,500 and $10,000 and at more than 60.0% for workers with income between $10,000 and $20,000. In 1972, the yearly maximum pensionable earnings was set at $5,500 under the Canada/Quebec Pension Plan.

The recent wave of inflation, which has forced governments to escalate all state pensions according to increases in the cost of living, has also brought pressure to do something about private pension benefits. In view of the fact that those benefits are not generally increased with the cost of living, the government has made the first $1,000 of private pension income tax-exempt. A similar exemption also applies to investment income. Both these measures are generally available and are not limited to those at retirement age at the time the measure was introduced.

The combination of these measures means that a retired couple may have an annual income well in excess of $8,000 before paying any income tax. These measures have produced a combined fiscal and social security system which is well harmonized. Even with the 50% tax-back rate of the guaranteed income supplement, no Canadian taxpayer over 65 can at the same time pay income tax and be eligible to receive the guaranteed income supplement.

The level of support guaranteed to older Canadians is thought to be above the subsistence level. Although this is true for both the single individual and the couple (if both spouses are above age 65), the income guaranteed to the couple is relatively more generous.

To this elaborated income security system, we must add a universal hospital and medical insurance plan for all Canadian residents. According to statistics available for Quebec, 23% of all expenditures under this plan were for persons of 65 years of age and over, although these persons represent only about 7% of the population. In Quebec this plan is completed by a drug assistance program providing free prescription drugs to those older people eligible to receive the guaranteed income supplement.

This picture of social policy for the elderly, although incomplete, does indicate that our concern as a society has centered, for the most part, on the satisfaction of the primary needs of older people with a concurrent neglect of secondary needs. These secondary needs which include companionship, sociality and social participation are just beginning to attract the attention of social planners. More often than not programs currently in existence or in the planning process are based on making a service in kind available rather than increasing financial assistance to the elderly.

Domiciliary services for the aged are scheduled for rapid development in future years. Such programs satisfy primary as well as secondary needs. A visiting nurse will provide security as well as companionship to the older person who continues to live at home. Such services have just begun to attract government funding on our side of the border.

A few years ago, the Federal government launched a new program called "New Horizons", the main objective of which was to provide an activity run by retired people in which they can use their talents, experience and energies 6/. These projects, to be accepted, must reach out to as many retired people as possible and answer a community need if they are to be accepted. The program is still fairly limited in scope since its budget in the fiscal year just ended was limited to $10 millions.

The Quebec government is currently promoting the creation of day centres, either within a reception centre for older people or at the community level.

6/ Health and Welfare Canada, New Horizons is...

If operated through a reception centre, the day centre would enable old people, admitted for a few daily sessions a week, to satisfy some of their health, social, and leisure needs. Only one or two such day centres are in operation at the moment.

Even with this large variety of programs, I am still tempted to ask the question: Are we right to force people to retire at 65? Would it not be preferable to spend a larger proportion of our resources on providing older people with meaningful work over a longer period of time?

MR. ROBERT F. LINK: Almost the whole structure of social and financial institutions for retired people has been put in place during my lifetime. Think of Social Security, including Medicare; private group retirement plans; mutual funds; nursing homes; leisure villages; condominiums; senior citizens; etc. One might reflect on whether this all represents a coherent design, or to what extent it reflects independent efforts plus the invisible hand of social, economic, and demographic forces.

While we're looking back fifty or more years, let's look back ten million years. What then passed for human society was very likely unable to support aged nonproducers. Then we pass to cavemen and early farmers, where the aged were probably supported by a sharing of group resources. Only in the relatively recent past has the dominant arrangement been one under which the aged tend to be separated from the rest of us and to be supported through separate cash flow streams.

The Institute of Life Insurance has been commenting lately on the growing "psychology of entitlement" -- the feeling people have that society owes them an income, decent housing, comprehensive medical care, etc. Maybe there is also some psychology of obligation -- a feeling that human life is sacred and should be preserved at all costs, followed by the idea that it should be a comfortable life. These changes have come on us so fast, it is not surprising if there are some pains and dislocations.

The "retirement needs of a population" covers several areas. There are the needs of the retired population itself. There are the needs of the active population looking forward to retirement. There are the needs of the entire population in dealing with the allocation of goods and services between producers as a group and nonproducers, including the aged, as a group.

The other panelists will talk about financing questions, so I don't want to get into this deeply. Maybe two quick observations.

First: There are signs that the present provisions for the retired population are often inadequate. We may have to deal with increasing future costs on this account. This may cause a strain if standard of living fails to increase in the future as it did until recently.

Second: The goods and services demands of the retired population will also rise because the retired population will be increasing relative to the rest of us, particularly in the early part of the next century. There is a tremendous challenge in this prospect. The scenarios that show an increasing per capita burden for retired people also show a reducing per capita burden for dependent children. Looking just at numbers, the dependent population may become <u>smaller</u> relative to the producing population when all groups are taken into account. The challenge is how to make a meaningful connection between these two trends -- increasing aged and decreasing children -- so that we pass some of the dividend from lower fertility on in some way to the retired instead of automatically channeling it into increased personal consumption. Two facets of connecting these trends should be mentioned. First, the trends may not be synchronized -- the decreased per capita burden for dependent children may precede the increased burden for retirees. Second, the concept of zero population growth, which is tied to this decreasing expense for dependent children, also means elimination of the costs of providing for an ever-increasing population, a factor sometimes called the "demographic investment" of society.

Let's look at the needs of the retired population now. We can sweep in the retirement needs of the active population as we go along. For a rough check list, we can use Abraham Maslow's hierarchy of needs. This crops up in books on personnel management. Maslow lists five needs. A person doesn't worry about number two until number one is under control; he goes after number three only when number two is pinned down; and so on. The needs are (i) survival, (ii) safety and security, (iii) sociality and affiliation, (iv) ego and esteem, and (v) self-fulfillment and self-actualization. I don't find the lines between these entirely clear, but let's go ahead and look at them briefly.

Survival involves needs in the here and now, primarily food, shelter, and maybe some degree of comfort and other amenities. Safety and security have to do with the expectation that the survival elements will continue to be available and that survival will not be interrupted by death, injury, or other unpleasant events. You can decide whether to put medical care in the first category or the second.

Some major institutions that pertain to this area are welfare and public assistance programs; Social Security; private retirement provision in money terms, including group plans; nursing homes; and leisure villages. It is not hard to find imperfections in this collection. There has been a good deal in the news lately suggesting that nursing homes may be in a lot of trouble, or perhaps that the people in them are in a lot of trouble. Social Security seems to be doing its job pretty well. Private retirement plans have done a tremendous job. However, since we want them to act as a backbone of private retirement provision, it's in order to look at them critically.

Retirement plans generally do exactly what they are designed to do, for people who retire after a full term of active coverage under one plan. But consider the gaps: (i) Inflation can ruin the benefits under most plans. (ii) Vested benefits carried from former plans tend to be inadequate. Full coverage under a series of plans is normally not as adequate as coverage under one plan. (iii) Even with the vesting rules in ERISA, there will be a lot of coverage that will never confer any benefits.

Think about vesting for a moment. The Arthur Stedry Hansen study showed that two-thirds of those in the plans covered would get benefits. No one mentioned a second inference from this study. Two-thirds of those covered by the plans in the study -- not the same two-thirds -- didn't know whether or not they would get benefits, because they weren't yet vested.

One viewpoint is that there are two polar choices of how a pension plan should work. At one extreme is the money purchase plan, including an opportunity for common stock investment. Such plans usually have very early vesting; they create full reserves; they heap up maximum interest yield by having relatively high contributions in the early years. The money purchase plan effectively turns the contribution over to the individual, with some benefit of group operational scale advantages; the individual then becomes the captain of his own economic fate. He gets the profits; he suffers the losses; but he knows where he is at. There is of course a crucial operational problem on past service.

A definite benefit plan, on the other hand, has the nature of a private social security system. One could argue that, where the plan sponsor controls the funds and benefits, there is a special duty to make sure that the system really works. This involves things like cost-of-living indexing of benefits, including vested benefits for employees who have left service; participation of vested and retired employees in plan improvements brought about by economic factors, etc. Let me quickly clap the lid back on this can of worms.

Summarizing up to this point, it is amazing that institutions brought into being in so short a time should do so large a job as well as they do. However, there is plenty of room for thoughtful improvement.

Let's go on to Maslow's remaining needs: Sociality and affiliation; ego and esteem; and self-fulfillment and self-actualization. Maybe we can do them all together. For starters, here is a quote from a May 13 Op-Ed item in the New York Times. Fred Hechinger, in a piece called "Silent Winter" said the following:

> "Nursing Home horrors could not have continued so long if even a moderate number of people had cared about what happened to the old. The fact is that the fate of old people is of little interest to the majority and an inconvenience to a large proportion of the families of the aged."

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> "Those who dreamed up the term 'senior citizens' were engaged in a cover-up of the problems of old age.

> "The high cost of space in modern urban apartments and the modern American family's mobility offer rational excuses for an ever-increasing reliance on others to assume responsibility for the aged. The pragmatic sociology of post-industrial urban America makes a virtue of segregating the generations. Children, teen-agers, young adults, the 'mature' (read: middle-aged) and 'senior citizens' are lured into, or confined to, their own worlds, their own literature, and their own potential for commercial exploitation."

Maybe Hechinger is overstating the case. But there is really something there. There does seem to be a tendency, probably increasing, for us to separate the retired aged from the rest of us. In typical situations, people cross the grim divide from producing to nonproducing status with a leap and a dull thud. Often they get what they want, particularly when they move to Florida or to a comfortable leisure village. But we all know aged persons who want to continue to contribute in some way; and we all know how the rest of us sometimes make it hard for them to do that.

Maybe I'm being too critical. But while we're at it, let's look at one other thing. We are possibly at a transition point between a time of adequate or abundant resources and a future time of scarcer resources. Further increases in standard of living may be much harder to come by. In the extreme, large changes in life-style may be needed. What does all this mean, if anything? We can improve the institutions we have -- clean up the nursing homes, make retirement plans work even better, be nicer to the aged, etc. There is a price; it must mean less goods and services for the rest of us. This is a reasonable task for many of us here; our occupation revolves around retirement plans and the whole concept of retirement. It's a worthy challenge.

However, in passing, we might ask ourselves whether the very concepts of retirement that have developed over the last fifty or one hundred years don't need reexamination. Maybe we need to reverse the process of segmentation. Maybe we need ways to reduce the economic burden of the retired by bringing them back among us, by making them as productive as they are able to be, and, in short, by giving fuller thought to the whole spectrum of Maslow needs.

MR. AVON GUY SHANNON, JR.: Most discussions of such a broad topic are qualitative. However, I think it is interesting, and sometimes sobering, to quantify the discussion somewhat. Certainly, no realistic discussion of meeting a population's retirement needs can take place without some understanding of the significant limits on resources available for this purpose.

For discussion purposes, I would like to consider various figures for 1972, the last year for which comparable figures are readily at hand. Subsequent inflation has changed the dollar levels, of course, but the basic relationships have probably not changed very much.

In 1972, total contributions for all retirement purposes came to about $20 billion dollars for private pension plans, $16 billion dollars for governmental plans, and $43 billion dollars for Social Security, or a total of nearly $80 billion dollars. Incidentally, benefits paid from these plans during 1972 came to about $67 billion dollars, so shifting to a pay-as-you-go basis for all plans would add less than 20% to the level of benefits currently being paid unless the reserves of existing plans are used up.

How does the $80 billion dollars currently being set aside for retirement benefits compare with current needs? If you define a moderate target benefit as 50% of final earnings at time of retirement for all employees, including the half of the population not covered by a private pension plan, the <u>additional</u> annual contribution required on a pay-as-you-go basis might be in the neighborhood of $60 billion dollars, at 1972 levels.

Where could such an amount come from? One source would be an increase in Social Security taxes. In order to provide an extra $60 billion, these would have to be more than doubled, from a current total of about 12% to perhaps 26% of taxable payroll.

The missing $60 billion might come from general revenues. In terms of the 1976 federal budget currently under discussion, this would involve adding roughly 20% to the budget, or doubling the projected deficit.

The extra $60 billion might come from a reduction in capital investment. For many years, capital investment has been fairly stable at about 10% of the GNP, or some $130 billion dollars for 1972. The extra $60 billion could be provided if capital spending is roughly cut in half. Of course, some economists are currently arguing that our total capital investment must be increased if we are to remain competitive in the world economy.

In relation to the total 1972 GNP of $1.3 trillion dollars, current pension contributions are about 6% of GNP. If we were to provide half pay at age 65 for all workers, 11% of GNP would be needed. Of course, many retirement plans provide much more generous benefits than half pay at 65. Moving to desirable benefit level by the standards currently being used for major corporate, union, or governmental pension plans, the cost would be considerably higher, perhaps 20% of GNP.

These numbers are rough, but I believe they are sufficient to identify the quantitative problem. By current standards, available resources fall far short of retirement needs, even when these are modestly defined. These figures were deliberately drawn on a static basis, since the gap between resources and objectives is so large on a current pay-as-you-go basis. If you care to project future demographic trends, changes in the cost of energy and raw materials, and increasing demands for goods and services, the $60 billion gap widens rather quickly.

If available assets are so limited, how can the population's retirement needs be met? Three types of change are possible. The GNP might be increased, the percentage of the GNP allocated for retirement purposes might be increased, or the retirement needs themselves might be redefined at a lower level. For example, existing resources would be much more likely to do the job if the normal retirement age were immediately shifted from 65 to 70. Since no such drastic change is likely, we should keep this quantitative problem firmly in mind in discussing a population's retirement needs.

MR. STANLEY R. FREILICH: Mr. Shannon's remarks seem to ignore the private savings factor.

MR. SHANNON: This is correct, although the magnitude of this factor should not affect the general thrust of the argument.

MR. GARCIA: Although I have no direct figures on this point, the experience of British Columbia in applying an asset test to reduce government pension benefits has been that only about 20% of the population own sufficient assets to cause a reduction.

MR. CHARLES B. H. WATSON: If a population's retirement cost projection is not affordable in terms of their gross national product, what is the solution?

MR. LINK: Perhaps the solution to an "entitlement philosophy" which leaves us drowning in an aged population is to integrate the aged into productivity.

MR. ROBERT J. MYERS: Why was the earnings test removed from the Canada/Quebec Pension Plan this year? This can run counter to the goal of more employment if employers believe the government is advocating retirement for virtually all employees at age 65.

MR. GARCIA: The elimination of the earnings test has occurred in Canada but not in Quebec, and may be motivated by political considerations. If the result is to reduce the actual number of retirees, the program may not be so expensive.

MR. DONALD S. GRUBBS, JR.: The basic need of retired people as for all of us is to have a livable world. In the 12 months ending in February of this year, births exceeded deaths in the United States by 1,200,000 persons. There was also substantial net immigration, much of it illegal. The population growth problems of most of the rest of the world are much more severe than in the United States. Any way you allocate resources, in a world with limited resources, growing population means less resources per person. We simply must face and solve this problem. Actuaries understand demography and exponential growth and should take an active part in striving for a solution. Some may want to become involved in organizations working on this problem, such as Zero Population Growth.

Guy Shannon has estimated that the United States needs to allocate at least an additional $60 billion annually toward minimum needs. Where could the money come from? We need to reevaluate our nation's allocation of resources. In particular, we should look at the $80 billion spent annually on the military budget. Beyond this, we need to do broad thinking about changing a world situation which calls for military expenditures of this magnitude. We must substantially strengthen the United Nations to the point where it can provide all peoples of the world with security, and then we will be able to redirect most of that $80 billion to human needs.

CHAIRMAN HOWARD YOUNG: Several people are suggesting bringing older people back into the work force, perhaps by increasing the retirement age, as a possible solution to the "burden" which the greater proportion of older people would create. However, if our basic long-term problem will be diminishing supplies of natural resources and energy, I'm not sure that enlarging the work force makes sense. The usual purpose of having more workers is to produce more goods and services, but that would mean consuming more, rather than less, resources and energy. Similarly, the idea of increased investment now to achieve greater productivity in the future would imply either fewer workers or more consumption in the future. The point is that the problem is how to distribute the output that is produced, but not necessarily to increase the output. Our usual concept is that distribution is related to current employment, or income from investments; any other distribution (e.g., Social Security payments) is seen as a "burden." Perhaps we have to rethink that concept.

MR. LINK: Use of human energy may cut the use of artificial energy.

MR. SHANNON: I'm reminded of a science-fiction yarn in which this problem was solved by countervailing productivity: half the population worked to undo the work of the other half. Rather than goods production, the development of the services market may be the answer.

MR. LEROY B. PARKS, JR.: One system of providing capital to retirees would be to mortgage their homes in exchange for annuities.

MR. MYERS: I do not want to discourage Mr. Parks, but just such an idea was developed by the Federal Housing Administration in the mid-1950's. Unfortunately -- since I agree that this is an excellent approach in the economic security field in the individual-savings sector -- the idea never took hold. I believe that this was the case, because people generally do not like the idea of having a lien placed on their home which prevents the home from being passed on to their children.

MR. GARCIA: In British Columbia, the government has recently instituted a program of paying the property tax on a house and, in return, placing a lien on the home. The issue of political saleability will become paramount when the first home ownerships are lost.

MR. M. DAVID R. BROWN: Many years ago, Bill Anderson foresaw the commercial possibilities for insurance companies in this concept; his phrase was to "annuitize" the house. The commercial basis may avoid political overtones.