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NATIONAL POLICY ON RETIREMENT IN THE UNITED STATES AND CANADA

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Public policy with respect to retirement matters has been actively discussed in both countries. Both the President's Commission and the Royal Commission have raised several key issues.

1. What should the role of private pension plans be in relation to Social Security and other public retirement systems? In particular, should a second layer or advance funded pensions be required?

2. Now that flexible retirement is recognized as a socially desirable goal, what changes should be made in pension programs?

3. What level of pre-retirement disposable income should be replaced by all forms of retirement benefits as a desired retirement income goal?

4. What changes should be made in the current tax policy regarding employee contributions, benefit payments, Social Security and private savings?

5. Is the present general approach to retirement program regulation sound and productive?

MR. COOPER: Canada and the US have both gone through extensive studies on national pension policy. In this country the President's Commission on Pension Policy has been at work over the past few years. The Employee Benefit Research Institute (EBRI) has been involved in this activity, as well as the ERISA Industry Committee (ERIC), and the Association of Private Pension and Welfare Plans (APPWP). There have been legislative efforts to improve the pension system both in the public and private sector. In Canada, there have been a number of studies undertaken as well. The first one that was completed was called Cofirentes Plus undertaken in the Province of Quebec. The Economic Council of Canada completed a study in 1979. The Federal Task Force, otherwise referred to as the Lazar Study, completed a study recently. There was a study by the Senate Committee on retirement age. There was a study by the Financial Executive Research Foundation of Canada which ended up in the form of a book and the Royal Commission on the Status of Pensions in Ontario just recently completed its study. Now these studies all have had and will have an impact on the shaping of pension policy in both countries.

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MR. BASSETT: It's a real pleasure to be here this morning and to talk to you about a topic that has taken up the last 30 years of my life but more importantly the last 2 years as I've worked with the President's Commission on Pension Policy. Actually I would like to adopt another name for it. Dallas Salisbury, who will be speaking later, is the first person I've heard use it. He calls it Carter's Commission on Pension Policy. I think this is a better description because I don't think our current President would like to be associated too closely with the recommendations of this Committee.

The Committee was set up by President Carter. There were 11 members on the Commission. None of them had any extensive background in pensions. The one with the most knowledge was Bill Grenold, who as many of you know was past chairman of TIAA - CREF, although his background was in defined contribution type plans and he was not too up to snuff on defined benefit plans. The next most knowledgeable person was Martha Griffith, a former Congresswoman from Michigan who had worked in the area of ERISA and EEOC but who had certain things that she wanted to see done. Industry was represented principally by Peter McCullough from Xerox who was chairman. I'm not going to describe the whole Committee - I merely wish to give you the flavor. They were business people mainly. They were not pension experts. The staff was completely recruited from within the Government. I was the only non-government person associated with the staff as well as being the only Actuary.

The purpose of the study was set out by legislation from Congress at the direction of President Carter. It was to establish a policy to guide the Government in taking care of the retired, disabled and survivors in the United States into the next century. They wanted to look at the problems through to the Year 2050 or so, so we could take care of what is known as the "Baby Boom" which is now entering our work force.

I'm going to talk about the three most controversial items in our report. One is the minimum universal pension system which has the acronym of MUPS. Second, I'm going to talk about our recommendations in regard to the age of retirement and finally the third topic I'll touch on is the tax structure that we're recommending. Before I get into those in detail I have to talk a little bit about our starting point. We early established what we thought were reasonable goals for retirement income. We said that from all sources people should try and the government should encourage them to have income to maintain their standard of living in retirement. We had some discussion on whether they should maintain their full standard of living or whether they couldn't cut back on their standard of living, but we felt a lot of the people were probably not in a position where they could cut back their standard of living very much. So we decided the goal should be **maintenance** of standard of living in post-retirement years. This was to be met through three different sources. The basic being Social Security, your Government sponsored program, the second being through the private pensions and the third being through individual effort, either from savings from prior years or continued employment in retirement. We left it that the individual was to have an important role in reaching this goal of maintaining standard of living. Then we made a little study to determine where things were

today. The goals that we set meant that (as far as relationship to gross pay because we had to take out taxes and work-related expenses and so forth) the replacement rate for the low paid should be about 80%, for the average paid about 65%, and for the high paid about 55%. If you're married you need another 5%. Then we took a look at what Social Security provided and we found there was a significant gap particularly for the single workers. Married couples where both spouses worked also had a gap. There was no gap for a married couple earning up to about the average wage. We found that Social Security pretty well took care of that group. Another problem area is that there is a significant group that does not have Social Security protection. About 90% of the population is covered by Social Security. The 10% that aren't covered are mainly in the Government. Civil Service employees do not come under Social Security, and about 30% of State and Local employees don't come under Social Security. You can say they have their own plans so there is no gap. But the gap occurs when there is movement, when a person leaves Civil Service, goes into private employment or vice-versa. They don't have the Social Security that flows with it so there is a gap from lack of universal coverage. There is also the problem of termination of employment with unvested rights or even vested rights in an inflationary economy where those vested benefits are frozen. We found that there is a lack of protection for spouses. In spite of ERISA legislation there are still in practice many spouses that find out after the death of the breadwinner they're lacking in adequate income. So those were areas where the private plan had failed to take care of the problem. On personal savings, there's strong evidence all through our report of encouragement of private savings. They feel that this should be encouraged in every way possible through favorable tax treatment. However, they did not come out in favor of mandatory savings. They also feel that there should be greater encouragement for older people to stay in the labor force and opposition to the trend towards earlier and earlier retirement.

One of their basic decisions was that there should be no more emphasis on transfer type benefits, where one generation pays for the benefits of another generation. In other words, they said let's have no further expansion of Social Security. It's having a difficult problem meeting its current and prospective financial commitments, so they came out strongly opposed to any further reliance on transfer type benefits through Social Security and Welfare. They also felt another reason is that there is need for more capital formation in the United States and therefore we should encourage the growth of capital through the pension route and not through the Social Security route.

Now let's turn to the specifics. The first I'll talk about is retirement age. Our first step was to recommend that the retirement age for Social Security be increased to age 68. The recommendation was that starting in 1990 it be increased to 65 1/4; in 1991 to 65 1/2 and gradually increase so that by the Year 2002 it reaches age 68. It will be necessary to amend ERISA to allow normal retirement age to follow that of Social Security. They recommended that the Federal Civil Service and other Federal programs immediately change their normal retirement age to 65 and then move with Social Security to age 68. The Federal Civil Service retirement age is 55 with 20 years of service.

Another topic was tax structure. They were concerned that there is a hodge-podge of tax treatment for monies that are set aside for savings or benefits that are paid in retirement. Some benefits are taxed, some benefits aren't taxed; some contributions are taxed, some contributions are not taxed. There are certain limitations for individuals who save for retirement, there are different limitations for other groups. All these ought to have a consistent tax policy. What they suggest is that all forms of savings for retirement be tax deductible whether to a private pension plan, to a savings account, or to Social Security. They went further to say that for low income people who would not have a tax deduction there should be a tax credit if that is more favorable. Of course, it could not be used as a lump sum payment. It would have to be frozen as ours are today. They even went so far as to say that no lump sum payments under pension plans or MUPS will be paid out unless they are under $500.00. These are savings to be set aside for benefits.

The more controversial item is our minimum manditory universal pension plan or MUPS. I'll briefly describe that plan to you. It would require that all companies that do not have pension plans put in a MUPS and those who have pension plans meet the minimum requirements of MUPS. This will be privately sponsored. It would apply to all workers in the United States who are age 25, have 1 year service, and work over 1,000 hours. It'll be full and immediate vesting and portable. Their proposal is for it to be a defined contribution plan, future service only, 3% of pay being set aside each year. However as a transition when the legislation becomes effective it will be 1% the first year, 2% the second and then 3% of pay thereafter. This will be accumulated in the individual accounts. It was proposed that a central clearing house be set up by a government agency to be available to employers who wanted to pay the 3% to the government rather than set up their own plan or to be a transfer agency for people who quit where the employer and the employee wanted the money transferred to this central clearing house. However, since all employers would have as a minimum MUPS, the amount could be transferred from one employer to another employer. It was suggested that perhaps the best agency to run it would be the Social Security Administration. There was to be committee set-up to handle investments. Investments of the funds would be in the private sector. The guide that they looked at was what is being done by the Pension Benefit Guaranty Corporation with funds that they take over on terminated pension plans where they have hired investment counsellors to invest the money. These contributions would be tax deductible to the employer and the tax rate in the United States varies by size of the company. The tax rate would be fixed at 46% for all these contributions. It looked like putting in this type of a program would fill about half of the gap that we saw in the present system for those who earned up to about the average wage. I explained earlier, for the married, one-worker family it more than fills the gap, while for the others it fills about half the gap. As I've said this is probably the most critical, most controversial proposal by the Commission. I'm still employed by the Commission so I'll keep my views for another three weeks and then after that I'll express my personal views. I will put down for your information what I seé as the negatives and the positives of this MUPS program.

On the negative side we have much more government interference in the running of business and in the way we compensate employees. There is no question that it will be an added labor cost. Who bears the cost? It's hard to say. There are certain indications that after a few years the additional 3% would be shifted largely to the employees through lower wage increases. But it is an added labor cost. It's inflationary. It may cause unemployment, lowered standard of living and all the other things that are connected with added labor costs. Another objection is that it's a fixed cost. It's not a function of profits, it's a fixed labor cost. Another negative is greater administrative costs. I think industry was a little relaxed about our MUPS because they said well we have a plan so we don't have a problem. They have a major problem. Every plan in the United States will have to be amended unless you have a defined contribution plan with full and immediate vesting with at least a 3% contribution and there are very few of those in the country. For example, a 3% accumulation would be available on a termination because of full and immediate vesting for a typical pension plan. That would mean anyone who terminates prior to age 50 will get the MUPS minimum benefit so you can see how important it is. I've made a little study and the cutoff point is at about age 50 where the typical plan vested benefits would exceed the value of a MUPS. All these have to be amended. There is going to be additional record keeping. I don't know quite how you would operate a MUPS if you have a plan in. I've almost come to the conclusion that you have to put in a MUPS with the plan and have kind of two coordinated plans because one's a defined contribution plan where you're going to have to give an allocation to individuals if they quit and to run that along with a defined benefit plan is a real administrative headache. Another negative is that it's a future service plan so it won't be beneficial to the employees for many years in the future. Then finally there will be a loss of government revenue because of the tax deduction. Pretty strong negatives but there are positive points.

It does meet the objective of bringing a large segment of our population up to what we feel is an adequate income. It certainly reduces the pressure to expand Social Security. It will encourage persons to remain in the labor force for a longer period of time. We hope it will increase incentives to save. It will increase capital formation. It will provide a more consistent tax policy and finally it will improve the financial problems of the Social Security system. I thank you.

MS. HALEY: I'm very **grateful** for the opportunity to speak to you this morning and to give you some insights on retirement income provision problems in Canada. Although it is true that the commission on which I served was an Ontario based one, in order for us to carry out our mandate we had to consider retirement income provision from both Federal and Provincial aspects and I think therefore I can give you some generalized remarks that apply to Canada as a whole. I was fascinated to hear what Pres Bassett had to say this morning about the Carter Commission. You will see that there is really a startling similarity between the Carter Commission recommendations and those of the Ontario Commission. I'd like to supply some factual background to put you into the Canadian picture. Retirement income for a Canadian 65 and over at the present time is provided from the following sources. First is the Universal Old Age

Security, which is payable at age 65 to all who meet the residence requirements. It is not earnings related in any way. The monthly payment is now $208.20 and this is escalated quarterly with increases in the Consumer Price Index. The second source is the Canada Pension Plan which is an earnings related plan. It is federally administered for all provinces except Quebec which has its own plan which is very similar to the Canada Pension Plan. It is done by agreement through the participating provinces. At the present time the contribution rates to the Canada Pension Plan are set at 3.6% of covered payroll, paid half by the employer and half by the employee. It also covers self-employed people who pay the total contribution. The contribution is made on earnings up to a yearly maximum pensionable earnings amount and this is currently $14,700. In time this will be equated with the average industrial wage for Canada which is now about $15,000. We would expect this to happen about the middle of the 1980's. Pension payments from the Canada Pension Plan are also escalated yearly to increases in the Consumer Price Index. The maximum monthly pension at this time is $274.31. Workers are required to contribute to this plan between 18 and 65 and pensions are available from age 65. There is no provision as there is in your Social Security for an early retirement option. The benefits under the plan are immediately vested and fully portable and no contributions may be withdrawn. The third source of retirement income is what we have called Employment Pension Plans in reference to both private sector plans and public sector plans. These plans are sponsored by an employer or a group of employers on a voluntary basis and although the exact coverage figures are in dispute, it is probably fair to say that somewhere between 40% and 60% of Canadian workers are covered.

In some provinces there is also an additional supplement to raise the level of guaranteed income payments to reflect in some way the cost of living structure in a particular province. So to sum up generally Canada is considered to have a three-tiered retirement income system: the Universal Old-Age Security, Canada Pension Plan, and employment pensions. Everything else is on an individual basis. The Royal Commission was appointed in April 1977 and was given a broad mandate to review all aspects of the provision of retirement income. Ontario is the largest of all the provinces in population and has been a leader in pension benefit design since 1965 when our Pension Benefits Act was passed. Ontario also has an effective veto on changes to the Canada Pension Plan and I will mention that again a little later.

As Keith has pointed out there have been a number of studies about various aspects of retirement income in Canada but I think the Royal Commission has been the most extensive in what it has undertaken. I think you'll be interested to hear what the main problems were as determined by the Commission and look at these against the background of the Carter Commission. First of all the current single, elderly person in Canada, and this applies particularly to women because of their longevity, is not receiving enough from government programs to insure a minimum level of retirement income to allow that person to participate in Canadian society. Married couples on the other hand are receiving adequate amounts and this arises primarily because of savings from shared accommodation and food purchasing. So there is a problem for the single, elderly person. Secondly, retirees who earned up to the average

industrial wage and who are receiving the full Canada Pension Plan payment but having no other income are still able to receive monies from the Guaranteed Income supplement. The Commission found it particularly unacceptable that a person should work all his or her lifetime and still end up receiving an income tested supplement from government. There are also in Ontario a million and a half workers (about 40% of the target population we were concerned with) who are neither members of an employment pension plan nor holders of a registered retirement savings plan. Although these are Ontario figures there's no reason to believe that a similar situation doesn't exist in the rest of the provinces in Canada. The fourth problem is that even if a person is in an Employment Pension Plan, a mobile employee under the present statutory vesting rule of 45 years old and 10 years service has a very small likelihood of receiving any pension money at all at retirement. In general, any break in service dramatically reduces the chance of providing through an Employment Pension replacement income which bears a reasonable relationship to earnings at retirement. I might just stress that the Commission was concerned with replacing a reasonable amount and would not have agreed with the Carter Commission that you must go for the whole works, the 100%. The fifth problem is that there is no rationalized system in Canada which fits together the various aspects of retirement income provision to deliver the needed benefits in an effective and a cost efficient manner. There is overlapping in the provisions. There is inequity of treatment among various classes of individuals and there is no consistent philosophy either in an approach to the fulfillment of the goals or in the statement of those goals themselves. The sixth and certainly not the last problem, but the last one that I want to touch on, is inflation. Inflation robs those in retirement of the real value of their savings whether these are characterized in employment pension plans, registered retirement savings plans or any of the less formal types of personal savings for retirement.

Now I'd like to point out what the Commission's philosophy was in approaching the solutions to these problems. The Commission believes that retirement income is the responsibility of the individual and that government has only a limited role to play in assisting the individual. The Commission also believes that government's responsibility is three-fold. First, to guarantee a minimum level of income in retirement below which no person's income should be allowed to fall. Second, to replace a measure of pre-retirement earnings in retirement. Third, to provide incentives for individuals savings for retirement. Do these things sound familiar? Once the government has fullfilled these three limited roles, then the Commission believes that the individual should be free to make his or her own choice between the levels of present consumption and the levels of future consumption and I think that's where our difference arises with the Carter Commission. We believe that there is an individual choice and if you do not choose to have 100% replacement in retirement that is up to the individual. Now it follows from this statement of the limited role the Commission sees for government that government should not be allowed to use the retirement income system or any elements in it to be a tool for controlling or directing other aspects of the economy for the government's purposes. This comes out particularly in the financing of the Canada Pension Plan which I will mention in a minute. So therefore premised on this philosophy which I've expressed the Commission has recommended the following: that government

(and that's either Federal or Provincial) now act to alleviate the problem of today's single elderly by increasing the minimum guaranteed income level and this could be done by increasing the payments under the Guaranteed Income Supplement. This is something that should be done now. The problem cannot be cured by something that takes effect over a long period of time. Secondly, we recommended that the government determine through the use of the net replacement ratio technique which would incorporate assessment of all forms of income and benefits such as free drug programs a suitable goal of net income replacement (we would say about 65% of the average industrial wage) and then design its programs according to such a goal. To this end the Commission sees the Old Age Security providing 10% to 15% of the average industrial wage in replacement, the Canada Pension Plan is providing 25% and then something that we have called PURS, the Provincial Universal Retirement System providing (that also sounds familiar) 20% of the AIW to provide a total from 50% to 60% of the average industrial wage. Those are gross figures because if you take these gross figures and work them through with the tax benefits for those who are below the average industrial wage we would see a net replacement level of well over 100%, and for those at the average industrial level what we would consider an adequate replacement. Once having provided these levels the Commission believes that those working above the average industrial wage are in a position to save and that the government should provide vehicles for saving to encourage savings through tax deductibility. Now let me talk just briefly about PURS (like the expression "Put money in your purse"). This is particularly designed as an answer to the current thrust from labor to double the benefits under the Canada Pension Plan to 50% of the average industrial wage. The Commission opposes this because of the problems with financing even the existing benefits. I might just say that Pete Cooper was responsible for the design of the projections that the Commission undertook for the Canada Pension Plan and it was a very fine piece of work if any of you are interested in having a look at it. Problems with the Canada Pension Plan of course are made more difficult by Canada's changing demographics. At the present time the proportion of old people to the working population is about 15.6%. By 2020 this will have risen to 25% if the current birth rates continued. Contributions for the existing benefits on a pay as you go basis are estimated to be about 9.28% of covered payroll by the Year 2030. Therefore doubling the benefits will inevitably have the problem of costing 18% for these benefits. Fully funding the Canada Pension Plan was considered and although this might provide a method of controlling the future costs, the difficulties of controlling the huge pool of money which would result made the Commission seek other approaches for the provision of this additional 20% to 25% of the average industrial wage. The PURS Plan provides for it on a fully funded basis with all of the funds allocated through the private capital markets in such a way that there can be no government interference or control. The PURS Plan has the following elements: a money purchase or a defined contribution design, it's earnings related but only on earnings up to the average industrial wage and here is the divergence from the MUPS Plan. It is employer-employee contributory with the contribution levels determined by what the government decides the replacement amount should be. In our projections we use a 2% employer contribution and a 1% to 2% age graded contribution for employees. Employees from age 45 on would be also paying 2%. It would be compulsory for all workers between 18 and 65 to coincide with

the present base for the Canada Pension Plan. The monies would be immediately vested and locked in and it would be fully portable though the extent of that portability would depend on the agreement of other provinces to institute similar plans. In that respect you have to realize we were a provincial commission and we had an obligation to come up with provincial solutions. There is no reason why such a money purchase plan could not be operated on a federal basis. An interesting feature is that the individual would have some say in the choice of financial mediaries for the investment of the funds in the private market. The plan would be fully funded at all times. The benefit would be a life annuity from the age 65, which could be postponed to 71, with survivor benefits unless the spouse consents otherwise and there would be no early retirement provision to have a benefit before 65. Finally, for employers having an employment pension with a similar fully funded benefit there would be an opportunity to opt out. So there we have a scheme that is very similar to the MUPS but limited so we do have difference in our philosophy there. But in any case we would see that with the PURS Plan, Employment Pensions as they now stand would continue on the same voluntary basis. So we have recommended a four-tiered plan: Old Age Security, Canada Pension Plan, PURS and the Employment Pension (RRSP) or whatever other vehicle the person might choose.

Finally as far as inflation is concerned the Commission recommended that there be no mandatory indexing in any Employment Pension Plan. We would only go as far as requiring that there be an option for a participating annuity in each employment pension plan. But we were concerned that there is a great deal of concentration on the indexing problem relating only to employment pension plans while other people in retirement are suffering the same loss of purchasing power from inflation. We had some doubts that full indexing in any case was necessary because both the Old Age Security and the Canada Pension Plan are fully indexed to increases in the Consumer Price Index. We were concerned that PURS, however, should be protected and so we recommended an inflation tax credit. This is a refundable tax credit administered through the income tax system. The way it works is that protection would be given to a narrow band of income above the government benefits for income derived from the PURS annuity, Registered Retirement Savings Plans Annuities, Employment Pension Benefits and other privately acquired annuities. This band we would suggest might be $11,500 in the Year 1980 and the credit would be available from age 68 in an attempt to use the mortality to make the problem less costly and to allow everybody to bear some part of the inflation problem. The credit would be determined by multiplying the eligible income by the increase in the Consumer Price Index and the multiplier would be cumulative for years after age 68. There is no doubt that it's an expensive proposal depending of course on the limits of the amount of income protected and the degree to which the rise in the Consumer Price Index would be used. We have no official reaction to this either at the federal or the provincial level at the present time but again I say that we are concerned that any solution which is going to require government action must take into account those who are less fortunate than those who are already in Employment Pension Plans. The time for talking about problems in Canada is coming to an end. Pension rights are within the legislative jurisdiction of the provinces and the federal government can only act if jurisdiction is accorded to it by the provinces. This was what was done for the Old Age Security and the

Canada Pension Plan. The federal government recently sponsored a National Pension Conference and it has suggested that its objectives for pension reform will be presented to the provinces in July 1981. The Treasurer of Ontario who is equivalent to the Minister of Finance for Ontario has already reminded the Federal Government that the jurisdiction is primarily provincial. He has also declared himself publicly as being opposed to any expansion of the Canada Pension Plan and he is giving his support to some move towards uniformity by the provinces across Canada. Ontario has a veto on any changes to the Canada Pension Plan and I think is in a fairly strong position for bargaining about it. Provincial uniformity has been difficult in the past and we've moved out of line considerably in the last five years but it may be that the necessary fillip towards uniformity will arise from the existing constitutional impasse. So all in all it promises to be an interesting time for pension reform both in the United States and Canada.

MR. SALISBURY: On one comment that Pres Bassett made, I should set the record clear so that the individual who deserves credit is given his credit. The references in some written pieces I've made to the Carter Commission on Pension Policy came about as a result of having read a document that was issued by Jimmy Carter before he left the White House outlining his accomplishments while in office. One of the accomplishments that he pointed to was creation of the Carter Commission on Pension Policy. I feel that a former President should be given credit for the things that he deserves. I have decided that in the future it should be so referenced. I make that note because as recently as last Friday I was severely chastised by the executive director of the commission for politicizing it by referencing it as the Carter Commission instead of the President's Commission so if I sound defensive to a slight degree, I am. The environment in Washington that one is beginning to see in the benefits area is very much being overwhelmed by the current state of the economy and by the intense concentration of the Congress on economic considerations. The likelihood, therefore, for dramatic changes being implemented over the next one to two years is relatively slim, although there will be some changes. The likelihood of at least consideration of dramatic proposals in the two to three years after that is significant. I point that out because in my view this hiatus provides the private sector with an exceptional opportunity to marshal its resources, to prepare and document its own views so that it is in a position to take a very active role at the time that these issues are actively debated by the Congress and the Administration. A number of issues that in our research we are looking at and that both of the Commissions looked at as overriding are issues regarding the strength of the economy, what employment levels will be, productivity levels, and future real wage growth. Population patterns are exceptionally important particularly to the Social Security program but also in terms of life expectancy and benefit payment periods to all of our private retirement programs. Of particular importance and growing significance in an area which is beginning to really be given full and complete consideration (which the Canadian Commission obviously focused on) are changes in household patterns and individual patterns, divorce rates, two-earner families, the extended family and differentiations between what the one-income household needs for adequacy relative to a two-person household. These have tremendous implications for benefits in general

and in particular for pensions and retirement income in the years ahead. There were uncontrollable uncertainties in many of these factors. As **a result** of those uncertainties it's our view in outlining our own research program that special care should be taken in determining what the problems are and what the solutions are. An example of an area in which there should be a match is a judgment of the success or failure of the private retirement income system in meeting the needs it was set out to meet. The point which is most frequently used is the assessment of the coverage provided by that system and the participation and vesting levels provided. The President's Commission on Pension Policy outlined coverage and the lack thereof as the major problem facing retirement income in America. It's a point which our research indicates is exceptionally and dramatically overstated and if that is the central problem, then it is one that we should look at carefully. We should thoroughly understand that benefit entitlement is very much tied to employer and employee characteristics that do provide substantial individual choice. Firm age, firm assets, employee age, employee preferences for pensions over other forms of compensation, workers' stability and the employees' decision to work part time, on a temporary sporadic basis or full time all factor in. To try to raise a generalized solution to that may indeed appear and in fact be short-sighted. For purposes of public attention and public analysis ERISA was established in '74 after more than ten years of careful study and it set as the judgment factor for participation in private pension programs age 25, one year of service and more than half-time employment. The President's Commission focused extensively on the total work force in laying out and identifying coverage as a problem. In setting forward their proposal for MUPS the press noted they came back to this 25, 1 and 1,000 as the relevant population for consideration. What does that do to the problem of talking about the total population. Out of a total civilian work force of 94.4 million people only 49.7 meet this ERISA definition. When the population is narrowed to this relevant work force the coverage rate increases from 56% to 74% and the participation rate rises from 45% to over 68%. 55.7% of this relevant work force is currently vested in a benefit and of participants who have had more than ten years of service with their employer over 78% are currently vested in a benefit. More than 9.2% of the relevant work force held vested benefits in another pension plan and more than 14.3% that are not currently covered by an employer plan hold vested rights from previous employment. Private employers have moved towards providing a solid majority of workers with private pension benefits. Recent policy recommendations have been based upon an assessment that future growth in that base is exceptionally unlikely. So let us very briefly turn to what some of those factors that have led to that assessment have been. History and research show that pension plan formation and the likelihood of increased coverage and participation is a direct function of real wage growth for the individual. History and demographics also show us that going through one's working career, real wage growth for the individual worker is exceptionally likely. Yet the models which the President's Commission and the Department of Labor before it used to reach their conclusion that there was limited likelihood of significant future pension growth assumed that between now and 1995 there would be absolutely no real wage growth for any worker category or for individual workers in general. The result, since pension expansion is tied to real wage growth, is very low

pension expansion if you assume zero real wage growth. The second set of assessments the commission used to move in this direction were models which were dynamic. The problem with the numbers that ultimately came out is that they took those dynamic models and said we're going to run them dynamically but we're going to place parameters in them. They first ran models based on 1968 and 1974 data and parameterized it so that coverage could not expand more than about 3% above the 1974 level. They ran the model to 1995 and, magically, coverage by 1995 had only expanded by the 3% which was allowed by the model's parameters and they therefore reached a conclusion of no future growth. We have had those same models run again by the same contractors without the parameters built in and they indicate that without those parameters private pension growth by 1995 will expand to 27% above its current level. That is probably higher than will actually occur. The truth probably sits somewhere in between and it is that truth and that information and those parameters and those ranges which our research will seek to make available to public and private decision makers so that decisions on future retirement income policy can be based on a full and accurate picture.

Another problem in the way the President's commission projected coverage was that they based many of their projections on behavior immediately after ERISA. They have not looked much at behavior since. Pension plan growth was absolutely dramatic prior to the passage of ERISA. Yet net plan creation went from 54 thousand plans in 1974 to only 3,019 in 1976 and then back up slightly to 19,601 in 1977. By 1980, however, the most recently available data indicates that net plan creation had risen to 56,063 with a significant percentage being defined benefit plans. Also significant, since the work force segment where there is the greatest potential for growth is the small employer,was that in the defined contribution area the average new plan size was 43 participants. The average new plan size for a defined benefit plan was just under 80 participants. Showing that in contrast to many recent government published assumptions that the expectation of plan growth amongst small employers was unreasonable, in fact, the growth is substantial at the current time. The relationship of private plans and retirement income to other polices must also be a factor that is very heavily built into research and policy making. In the modeling which the pension commission did in terms of assessing the effect of the mandatory program, they made it very explicit that was the only thing they modeled. They did not build into that modeling any prospective changes in the Social Security system, or any prospective changes in other aspects of tax treatment. It was an exceptionally limited and partial analysis. Yet research available would indicate to us that such partial analysis will not lead us to constructive and whole polices. Research that is available shows that the Social Security program and payroll tax levels have had a dramatic effect on the private sector, on the makeup of the total compensation package and on the ability of the employers to create new plans. In 1950, the tax rate for Social Security was 3% of the first $3,000 in earnings. It has risen by 1980 to 12.26% on the first $25,900 in earnings. Now putting those both in constant 1967 dollars, it is only an increase from $6,000 to $10,335 but in real terms that still represents a significant increase and reduction in employer and employee dollars available for the determination of personal saving. In addition, one must look at the effect in recent research of other government policies such as the introduction of individual retirement accounts and

other savings on structured employer plan formation. To the degree that there is data available on situations where the employees have the ability to stop contributing to some other employer mechanism in order to form an IRA, the statistics indicate that movement has been substantial. So not only must we concern ourselves with the effect that public programs have on the ability of employers to provide retirement income, but we must also carefully look at the impact of public policies on individual private benefit provision and the impact this might have on employer sponsored plans. But in looking at all of these things and looking at the way coverage statistics (and the way in which they were reached is a problem) drive proposals for mandatory pensions and other proposals, one must conclude that the problem has been dramatically overstated in recent months and that the extant research and projects now being completed will show that the private sector will make substantial progress and that there is room for substantial additional expansion and that recent trends would indicate that that current expansion to a large degree will take place even in the setup of current tax and economic policies. That does not mean you do not want to consider other policies. It simply says you should not give as a reason for policy change a situation of ultimate disaster.

A second major issue which the program mentioned was the issue of inflation and its effect on retirement income programs. Its effect in terms of Social Security has been undeniable and it has pushed increases in the necessary tax rates and in congressional action. But the overriding economic concerns in Congress and the fact that those economic considerations will begin to drive public and private retirement policies is evidenced by the Senate budget committee's decision last week to recommend to Congress that the formula for indexing both Social Security and all other government programs be adjusted to the lower of wages and prices. There are members of the committee who are actively considering pushing that in addition an 80% cap of the lower of those be the indexing percentage. To the degree that the recognition comes about it will also in all likelihood pass over to pressure the private sectors. One area of study which we have not been able to find any work on and in which we hope to begin undertaking some work and which we feel employers need to begin looking at is the pressures for indexing either ad hoc or on regular basis. The pressure on a private retirement income program can be expected to be a direct function of the inflation level and if we see inflation continuing to go up then at what point do those pressures on the Congress for mandating action or on the employers in the collective bargaining situation to move towards automatic indexing become insurmountable. Coping with change is another area that we must undertake to look at. There are numerous facets of change which benefit planners must deal with. Social Security changes which would encourage flexibility such as raising the normal retirement age are an example. To our knowledge at this point, very little if any work has been done as to the impact on private employer plan sponsors of having Social Security's retirement age raised, particularly the effects and implications on those plans that provide supplemental benefits until the time that Social Security benefits are available. Uncontrollable employee and employer characteristics will have to be considered. Controllable environmental characteristics also contribute including inflation, productivity, and employment levels. Employers are beginning the process of adjustments in a number of ways including interest in flexible benefit programs,

increased interest in partial benefit adjustment to inflation, increased opportunity for part time retiree re-employment, increased provision of preretirement counselling, increased recognition of employee benefit planning administration as a central and vital financial function in the company, as well as increased emphasis on benefit program coordination. The pressures for that type of activity will only grow in the future and the need for the information base to make that work cost effective on a broad scale will only grow.

Government regulation was another area highlighted on the program. In terms of the assessment of government regulation, the research that is available clearly shows that it increases plan cost, increases uncertainty for plan sponsors and potential sponsors and dramatically limits employer flexibility. While it has positive effects as well, where it increases costs it nonetheless inhibits plan formation. The degree to which government regulatory changes over time inhibit plan formation should be considered in assessing the performance of the private sector. Tax incentives have had a noticeable positive effect on plan formation and new tax incentives in the form of deductible employee contributions are being currently considered, as are higher contributions for Keoghs, by the Congress. The degree, however, that one should begin to consider those changes in addition to the factors that are now being looked at is how those changes will compete for dollars with current retirement programs and how they may change employee desires in terms of programs provided by their employer. The diffusion of government regulation among numerous government agencies is another factor which has been the subject of much debate and much public and private study. Legislation will be introduced in the next few weeks to create a centralized government agency. It can be viewed in two different ways: as a negative because it increases compliance cost, and as a positive in that it limits the ability of the government to act in a fashion that is arbitrary and capricious. That balance, which is principally a political balance, is the one on which that decision will rest. Future prospects in this area are that the Congress will begin hearings soon. There is a hearing at the Finance Committee on May 15 to look at the report of the Carter Commission. There are series of bills that Claude Pepper in the House is putting in next week: one which would create a mandatory universal pension system, one which would provide first year vesting, and one would provide for an additional tax incentive. The legislation will begin to flow to enhance the level of public debates. The opportunity for the private sector to become involved will very much be there. For the private sector to become complacent based on the fact that we have a relatively conservative administration in place would probably be unsound. One only need to remember the image of conservatism of the Nixon and Ford administrations and the fact that it was through those administrations the Employee Retirement Income Security Act was formulated. Thank you.

MR. COOPER: I'd just like to comment on what we heard from Donna today about one major study in Canada. I would remind you that the recommendation of the Ontario commission about not expanding the Canadian Pension Plan is not a view that was stated by some other studies up there in which they push very heavily for expanding that program. While the President's Commission of the US talked about 100% replacement of after tax income, the Royal Commission did not, but other studies in Canada

did. I just mentioned that because there seem to be variations of opinion. One thing we did not dwell on too much today were tax incentives needed in this country to expand to a higher level of savings.