RECORD OF SOCIETY OF ACTUARIES
1982 VOL. 8 NO. 4

INTEGRATION OF PENSION PLANS — WHERE ARE WE HEADED?

*Moderator: CAROL W. PROFFER. Panelists: VINCENT AMOROSO, DONALD S. GRUBBS, JR., ELAINE WORDEN**

1. Current integration requirements - what is and what might be.

2. Problems with the current rules - need for change, or not.

3. The recent proposal by Congress to redesign integration rules - does it solve the problems or create more?

4. Practitioners' proposals to revise integration rules - in light of recent activity in Congress.

5. The next step - better or worse?

CAROL W. PROFFER: We will begin our session this afternoon with Vince Amoroso of PBGC. Vince will comment on our current integration requirements and how they evolved. Following Vince, Don Grubbs from Buck Consulting Actuaries will provide a practioner's viewpoint and look at some of the alternatives that need to be considered in integrating pension plans. Then, Elaine Worden, Legislative Attorney for the Joint Committee on Taxation, will discuss the changes which have been effectuated this last August and their effects on integration plus what we can anticipate seeing in the future and what we can anticipate working with.

VINCENT AMOROSO: A lot has happened in the two years since I wrote the transactions paper on integration. I'd like to take a few minutes to trace the discrimination standard that has been the foundation of the integration rules from 1943 through the publication of Revenue Ruling 71-446. Then I will touch on the integration proposal made by the Carter Administration in 1978 and the one made by Congressman Charles Rangel earlier this year. Finally, we will discuss how these proposals depart from the discrimination standard that has remained essentially intact for the past 40 years.

Treasury Regulation 111 established the standard for determining whether an integrated plan satisfied the anti-discrimination standard enacted by the Revenue Act of 1942. A new Act 5539 which was published in 1943 and Mimeograph 6641 published in 1951 provided the detailed elaborations of

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that standard. The regulatory standard provided that benefits could not be relatively and proportionately greater for employees earning above any specified salary amount than for those below such amount. The pertinent regulation was recast after the Internal Revenue Code was amended in 1954. Regulation Section 1.41-4 was published in 1956 and was amended last in 1963.

The current standard uses different words to convey the same message as its 1940's counterpart. It states, "A plan will not be considered discriminatory merely because the contributions or benefits bear a uniform relationship to compensation." The value of employer provided social security benefits is added to plan benefits in ascertaining whether a plan satisfies the prohibitive discrimination standard. Briefly, Mimeograph 6641, the 1951 standard, provided that an excess plan was properly integrated for tax qualification purposes so long as the plan benefit did not exceed 37-1/2% of average pay, (averaged over a period of at least 5 years) in excess of $3,600 for employees with at least 15 years of service at normal retirement. Reductions in this limit were required if the plan provided any so-called subsidized ancillary benefits. The corresponding unit benefit plan limits were 1-1/4% in excess of $3,600. for career average plans, and 5/6% for final average plans.

While these limits are virtually the same as the ones in Revenue Ruling 71-446, the rationale for them is not. The 37-1/2% in the 1951 standard was derived as follows: The maximum old age benefit under the 1950 Social Security Act was $80. per month, and this is 26-2/3% of the $3,600. annual taxable wage base. The value of total benefits was estimated as 150% of the primary old age benefit. The total value placed on social security benefits was determined as 150% of 26-2/3% or 40%. Whereas the ruling acknowledged that employers and employees contribute equally, employee contributions were assumed to buy a straight life benefit of only 2-1/2% of pay, so that 37-1/2% was derived as the difference between the total value of 40% and the value attributed to employee contributions of 2-1/2%.

As the Social Security Act was amended during the 1950's and early 1960's, additional rulings were published by the Internal Revenue Service. These intervening changes modified the value placed on employer provided social security benefits generally by increasing the value of the benefit attributed to employee contributions. In its 1963 reports the President's Committee on Corporate Pension Funds recommended that employers should be given credit for 50% of the total value of social security benefits. This recommendation did not address the general discrimination standard. Rather it was concerned with how the total value of social security benefits should be allocated between employers and employees. At about the same time the general level of social security benefits was increasing.

The Treasury Department and IRS reacted to these two developments by announcing that the prior practice for deriving the value of employee provided social security benefits would be abandoned. Henceforth the total value would be divided equally, and that criteria remains in effect today. Revenue Ruling 69-4 was the first total restructuring of the integration rules since its 1951 predecessor. It established 30% as the maximum integration level for pure excess plans. Following the 1971 social security benefit increases, IRS changed some of the factors in 69-4 but

retained the methodology which is described in Section 3 of my paper on integration. Revenue Ruling 71-446 has remained substantially unchanged since its publication. During the ERISA debate, Congress considered freezing the integration rules notwithstanding the changes in the underlying social security program. Instead, the legislative history instructed the IRS not to issue further rules until June 30, 1975 while the whole subject was given further thought.

Although not positive, this suggests that the issue is not closed. In 1978 the Carter Administration, through the Treasury Department, proposed a revamping of the integration rules. As many of you probably recall, the proposal would have banned pure excess plans. Instead the accrual rate for pay in excess of the bend point could not exceed 1.8 times the accrual rate for pay below the bend point. Earlier this year Congressman Charles Rangel introduced HR-6410. Among other things the bill addressed the integration rules. Under the Rangel proposal the integration rules would be revised so that plan benefits could be reduced by no more than the value of social security benefits directly attributable to the plan sponsor. Recognizing that recordkeeping could be difficult under that criteria, the bill also established a safe harbor. Benefit or contribution accrual rates for pay in the $30,000.-$60,000. range could not exceed two times the rate of accrual above or below the range.

There is a significant difference between these latest proposals and the regulatory anti-discrimination standard that has been in effect for some 40 years. Both of the proposed changes would have added benefit adequacy to the long standing requirement for equity. Excess plans would have been required to provide minimum benefits. The amount of minimum benefit would have increased with the excess benefit being provided. Although the Rangel integration provisions were not included in the Tax Equity and Fiscal Responsibility Act of 1982, TEFRA does require certain plans to provide minimum benefits. Top heavy plans must provide a minimum non-integrated benefit of 20% of pay for non-key employees with ten or more years of service. This TEFRA provision appears to address the same goals which presumably formed the basis for the Carter and Rangel integration proposals.

This may mean the long awaited overhaul in integration has been obviated, or it may mean that action has merely been deferred. After all, in its 1981 recommendations, the President's Commission on Pension Policy states, "the current integration rules may discourage the fulfillment of retirement income goals particularly for low wage earners." The top heavy rules address minimum benefits in the context of discrimination, but the President's Commission seemed to recommend that there is more to come.

DONALD S. GRUBBS, JR.: We are fortunate at this session to have had presented to us two outstanding papers: the first by Vince with a history of where we've been and how we got there with respect to IRS rules. The second very fine paper was presented by Mr. Chang and eleven co-authors. There is a very high correlation between the membership of these co-authors and the membership of the Society's pension committee this year and last year. It presents a specific proposal and suggests minimum benefits for all integrated plans. Stay tuned -- my guess is some changes in IRS rules or a basis for change in IRS rules and the rationale for

it. It provides a very fine technical analysis that is helpful to all of us whether we agree or disagree with their particular conclusions.

By definition, "integrate" means "to form into a whole, to unite so as to form a complete or perfect whole", and that is what we are trying to do when we integrate pension plans. First of all, we try to fit together social security and the private pension plan into a unity. But we try to integrate more than the private pension and social security. We try to bring together these two sources of income after retirement with the employee's compensation before retirement in order to "integrate" and provide a pattern of income during a worker's lifetime before and after retirement. It has a unity which makes sense for employees at all levels of income.

The Chang paper states, "The objective is to spread an individual's earnings from production during some 40 years of employment over a span of some 60 years or more". This can be done in such a way that the individual suffers no abrupt financial discontinuity during the transition from an active life to a retired life. I fully endorse that statement. I believe that this can most clearly be accomplished if aftertax income from social security and the private pension plan combined is equal to aftertax compensation before retirement. This should be the goal. The rational social policy behind integration should be to encourage employers to reach that goal as nearly as possible. It is this goal, meeting the needs of all American workers, that should be the driving force behind integration rather than discrimination.

The problems with the present IRS rules are widely recognized. They are four-fold: First, the rules are too complicated. As one who has tried to teach them and recalling my own struggles trying to learn them originally, I think we all can agree that there is just too much detail for people to understand. Second, they do not recognize the changes that took place in social security since the last Revenue Ruling was published. Most particularly they do not recognize the 1977 amendments which, for example, completely abolished the rational basis for covered compensation which is 12 times average monthly wage. No one's pension under social security is based on average monthly wage. The third problem is the rules are not fair. For someone hired at age 60 who retires at 65 an employer may offset his pension by 83-1/3% of his social security benefit even though most of that social security benefit was earned with prior employers. The fourth deficiency in the existing rules is that they don't really accomplish that social goal of providing people with income before and after retirement that provides a continuity. Here you see the objective which is to provide a same take home pay before and after retirement.

Before Retirement
Tax
Salary

After Retirement
Tax
Pension
Social Security

In each case there is a tax element. The tax element is smaller after retirement than before retirement, and it's the equal take home pay which is the important thing. What private plan benefit formula will accomplish this goal? Note that as income goes up the tax element of both columns becomes a greater proportion. In an exact approach it is far too complex for practical use. Table I of the Chang paper demonstrates that a formula of 80% of total earnings less 100% of the Primary Insurance Amount does a pretty good job at all levels of income. Thus, the 80% goal with 100% offset produces a result very close to the above illustration. I've made some calculations to adjust the Chang Table 1 to reflect changes in the tax rates since it was prepared and I found it still does a very good job, as fine as we might expect apart from some far more complex approach. Since 80% of final earnings less 100% of PIA accomplishes the social purpose of providing people with an aftertax income, during retirement, that equals the income before retirement so as to maintain their standard of living, this formula should be allowed and actively encouraged. Therefore the rules should be that a plan under which the benefit formula before offset is at least 80% of final earnings or final average pay over 5 years or less, should be allowed to offset for 100% of the PIA.

Many companies cannot afford a plan as rich as 80% minus 100% offset. Where should the cut be made if we cannot reach that goal? One possible approach would be to merely reduce the 80% benefit formula to a lower percent, but still apply a 100% offset. For example, consider a formula that provides 50% of final pay less 100% of PIA. This gives all retirees 50% of final pay which is 5/8 of the goal. It has to be said that the reduction from $8,000. to $5,000. of income for the low paid worker is far more difficult to adjust to than an adjustment from $80,000. to $50,000. for the high paid worker. Any cuts across the board make it far more difficult for the low paid worker to survive. In addition, for our low paid worker, a private plan may provide little or no income at all. A second approach is to reduce the offset proportionately to the reduction in the ideal 80% benefit. Thus, an 80% plan that had a 100% offset (i.e. one that the offset is 1.25 times the benefit formula) could lower the 80% as long as the offset did not exceed 1.25 times the benefit formula. For example, the plan could provide a benefit of 40% of final earnings minus 50% of PIA. This procedure would do a better job for people across the board in terms of their needs for income than the flat adjustment.

The 80%/100% rule is a good rule for an entire career, but what about shorter service. If 80%/100% would be a good basis for an entire working career as the Chang paper demonstrates, a reduction of 1/40th for less than 40 years makes sense. Pensions accumulated with several employers are more apt to do the job on that basis although we always have the problem of a deferred vested pension not keeping up with inflation. Therefore a unit credit approach of 2% of final earnings minus 2-1/2% of PIA would be ideal. What about benefits that begin before age 65? Actuarial reductions would seem to be appropriate. What about step-rate plans? Under step-rate plans, if the PIA equalled the same percent of the Average Indexed Monthly Earnings (AIME) at all levels of income, it would be easy to design an appropriate step-rate rule. Unfortunately, we know that's not true because of the bend points. There is no perfect solution. There are only relatively suitable solutions for step-rate plans.

The Chang paper shows that a step-rate plan with a breakpoint equal to AIME for the year before retirement, such as 40% below the breakpoint and any percent above the breakpoint, does a fairly good job of meeting the objective of providing an income after retirement equal to the income before retirement. If the employer cannot afford a step-rate plan this good, the same principal mentioned before seems appropriate.

I had mentioned that the rules suggested earlier would not require amendment to most existing plans. That has merit in itself. On a step-rate plan for short service employees, a 1/40th reduction for years less than 40 is a simple 1%/2% formula. I concur with the Chang paper that pensions under the private plan should be integrated with pensions under social security. It makes no sense to change the amount of pension under the private plan depending upon death benefits and disability benefits under either social security or the private plan. Disability benefits under the pension plan should be integrated with disability benefit under social security and death benefits under the private plan integrated with death benefits under social security. Similarly employee contributions in either the plan or social security are irrelevant to the question of providing the flow of income that meets employee needs and should be disregarded.

What do we do if the social security retirement age is increased from 65 to 68? Again, we need an integrated program to meet the needs. That means we need to integrate retirement ages, and the retirement age under the private plan should be increased from 65 to 68. But another kind of integration that is missing between private plans and social security is a cost of living adjustment after retirement. The problem here is that even though the benefits start out adequate, benefits which are not adjusted by the cost of living are in real dollars decreasing benefits. Therefore private sector plans need cost of living adjustments, but we know many of them cannot afford it. If, moreover, we increased the retirement age under the private plan from 65 to 68, we could afford to provide cost of living adjustments after retirement up to a maximum of 5% per year and this would be financed by the savings from the later retirement age. I think this should be required for those who choose to use a retirement age higher than age 65 and further that the anti-cutback rules of ERISA be modified to say that the employer who changes an accrued benefit from a level benefit at 65 to an indexed benefit at 68, a change which would better meet the needs of employees, should not be regarded as a violation in the anti-cutback rule.

Next year, Congress is considering vast changes in social security. Since we are talking about making the two programs fully integrated, I think it would be unwise to make any change at all before we get action by Congress on social security.

ELAINE WORDEN: Vince and Don have given you a good historical perspective on the purposes behind the integration limits that we've all come to work with in 71-446. Vince stressed the need to limit discrimination in favor of what used to be called the prohibitive group, and Don stressed the emphasis on providing adequate retirement income for all employees of the group. It seems to me that this summer Congress took the middle

ground without specifically addressing fully the discrimination issues and certainly without fully reaching the retirement income adequacy issues. They wanted to insure that rank and file employees or non-key employees got a bigger share of the pension pot.

The stage was set very early on this year; there were a lot of economic pressures relating to the horrible inflation we've all been suffering as well as the numerous rumors and threats regarding the solvency of the social security system. I think Mr. Rangel noted that we anticipated pension tax expenditures to rise to the level of about $127 billion. Noting that certain articles in legal publications suggested that ten or twenty percent of those pension tax expenditures go to the benefit of rank and file employees, he become somewhat distressed and began a course for pension reform. Mr. Rangel and many other members finally, but somewhat reluctantly, accepted the theory behind social security integration (i.e. social security benefits are in essence slanted towards the lower income workers so that it should be possible to spread plan contributions or plan benefits toward the higher income workers, as long as, in the aggregate non-discriminatory benefits were provided).

Let's go through the provisions of TEFRA and see what in fact, was achieved. TEFRA makes some integration changes both directly and indirectly. Directly, TEFRA changes all integration rules applicable to what used to be KEOGH or HR-10 plans and those rules applicable to defined contribution plans. Indirectly, as Vince noted, the top heavy provisions take away a lot of the pressure on either defined benefit or defined contribution integration in the context of a top heavy plan. Before TEFRA, if you had a KEOGH plan which covered an owner employee, and if it was a defined benefit KEOGH, no integration was permitted. If it was a defined contribution KEOGH plan covering owner employees, integration was very limited and the plan could not be integrated unless no more than 1/3 of the benefits went to the owner employees. If you met that test, you could only integrate, not up to the assumed 7% rates in 71-446, but merely be reducing plan contributions by the applicable OASDI tax rate. If you reduce the rank and file contributions by the actual OASDI tax rate, you had to reduce the benefit provided to the owner employee by the much higher self-employment tax rate.

TEFRA took this rule, and in a spirit of parity to provide uniform rules for plans maintained by both corporate and non-corporate employer, applied a modified version to all plans. Under TEFRA, a defined contribution plan would not be considered properly integrated unless the integration is limited to an amount equal to the OASDI tax rate in effect times the wages up to but not exceeding the taxable wage base. The taxable wage base is $32,400. A plan would be integrated on a purely excess basis if it merely provided for contributions equal to 5.4% of wages in excess of $32,400. The social security act has already scheduled percentage rate increases through 1990. Thereafter they are going to be at a flat 6.2% rate. But in no year yet scheduled will the actual OASDI rate equal or exceed the previously assumed 7% rate that we know in 71-446.

It is interesting to note that when TEFRA expanded this rule to all plans it dropped the concept of no more than 1/3 of the benefits or contributions going to the key employees and it dropped the requirement that

related to the rate under the Self Employment Contribution Act (SECA). Consequently, if you have a plan that covers owner employees you may integrate by subtracting 5.4% from each participant's plan contribution whether or not that individual is actually subject to the employer provided social security protection or the self-employment coverage under SECA.

Several other things are interesting to note: Under TEFRA the plan has to establish the wage base and the social security tax rate as though in effect on the first day of the plan year. Once TEFRA came up with that language and they added it in a new sub-section 401(l) of the Code as fairly detailed language rather than just in the general provisions of 401(a)(5), a lot of questions developed. Section 401(l), as currently drafted, is fairly rigid. It doesn't say you have to be non-discriminatory; it says the total of your computed social security contributions, the OASDI rate times wages up to the wage base, when added to the plan contributions on any individual's behalf, must bear a uniform relation to compensation. That's somewhat of a departure from the concepts of 71-446 which merely stressed a non-discriminatory relationship. We are somewhat at a loss in terms of what will happen and how this will be regulatorily imposed. Recent panels with Ira Cohen seemed to indicate that they envision on a prospective basis the same type of flexibility that we had under 71-446. Relying on the somewhat sketchy legislative history of the conference report, Ira notes that the purpose of this legislation was to decrease integration in a defined contribution plan without increasing any other integration. The idea is that, for example, you should (as you could before TEFRA) be permitted to integrate at a lower integration threshhold. That is an issue that has been with us since 1969. Using 71-446 for the moment, if you assume that the employer's cost of providing social security is really equal to 7% of the wages up to the wage base, the only time you'll come up with a uniform percentage of pay, both above and below the wage base, is if you use that wage base as your integration threshhold. If you use a lesser threshhold, the people with no compensation in excess of the threshhold (I'm going to say $20,000. for this example) will have no additional benefits. They'll have only the assumed 7%. Those between your $20,000. threshhold and $32,400. will definitely have more than 7%. They'll have 7% plus the incremental plan contribution. Those above $32,400. will have a much smaller, but marginally increased amount because they will have an additional percentage for the amount between the $20,000. threshhold and the $32,400. wage base. That hump is one that has been with us since 1969. At that time the integration threshhold was much lower and there was no argument that participants with earnings at that threshhold that could be highly compensated.

When they derived the 1971 Revenue Ruling, they considered the hump again and concluded that there was no argument of highly compensated, and no prohibitive discrimination. In the 1978 Carter proposals, however, for the first time, there was some concern that the wage base had increased to such an extent that it would be appropriate to eliminate the hump and the Carter proposals did that. TEFRA, however, did not directly address that issue and as I understand the current thinking of the IRS, TEFRA did not eliminate the hump. Can you integrate at a higher integration threshhold? Revenue Ruling 71-446 permitted this, but if you used a

threshhold higher than the taxable wage base they required that you reduce the percentage. This technique was possible under 71-446 because of the very general language under 401(a)(5). The technique would not be permitted under the literal language of new Section 401(l) because you are integrating an amount greater than the rate times the first $32,400. of wages. However, if you consider the change in the integration threshhold, what happens in most instances is that you are integrating or providing less benefits to those who are "highly compensated", so that there is no prohibitive discrimination.

The last very important issue that has surfaced with respect to the TEFRA changes is what to do in a target benefit plan? Under prior law you integrated a target benefit plan using a defined benefit offset and the excess formula. There is some question whether that would be permitted under TEFRA. There are a couple of alternatives. Because 401(l) literally applies to all defined contribution plans (and target benefit plans are defined contribution plans), there is some argument which suggests that you should force a target benefit plan to establish a non-integrated benefit formula and then reduce annual contributions by this 5.4% up to the taxable wage base. That would not only cause a marked departure from plan design in dealing with target benefits, but it would also have some unusual results depending upon the age and salary level of the employees involved. It may, in some instances, create greater integration. Accordingly, relying on the language in the Committee Report which states that "we're not intending to increase the integration in any other plan", it is presently IRS thinking that that alternative is not feasible. A second alternative and one that many in the industry have advocated, is that we continue target benefits as defined benefit plans, and permit them to use the 71-446 excess and offset formulas. That seems somewhat hard to reconcile with the literal requirements of 401(l) that change defined contribution plan integration. That result seems equally unpalatable to others. A third compromise is currently being explored which would start out by allowing a target benefit to use the defined benefit integration formulas. However, since those formulas under 71-446 were based on assumptions comparable to the 7% defined contribution assumption under 71-446, an argument is made that that defined benefit integration should be reduced by 7/9ths (7/9ths being the rough proration between the previously assumed 7% and the current statutorily imposed 5.4%). Based on Mr. Cohen's last conversation, the third alternative is the one that seems to be most consistent with the literal terms of the statute and the legislative intent in TEFRA.

In the defined benefit context there is only one direct change made by TEFRA. That would be KEOGH section 401(j). If you have a KEOGH plan then 71-446 applies. Use the normal integration formulas whether or not you cover an owner employee. Once TEFRA is fully in place, you will have no "401(j)". You will merely have a defined benefit plan covering a self-employed, or owner employed individual. More importantly, as Vince noted, TEFRA made some indirect changes in the integration area by requiring a minimum non-integrated benefit in any top heavy plan, whether the plan is defined contribution or defined benefit. The objective is to guarantee that rank and file employees get a bigger percentage of the pension pot.

When Mr. Rangel introduced HR-6410 he envisioned more radical revisions to the integration scheme, not only the defined contribution changes which were ultimately enacted in TEFRA, but also a fairly complicated defined benefit mechanism which would require that the employer keep track of accumulated OASDI contributions on behalf of any participant with interest to retirement. A procedure would have been provided to translate the accumulated balance into an equivalent benefit at the time of retirement. The testimony on HR-6410 regarding that integration change was overwhelming. Whether you were "excessively" or "abusively" integrated or not, that change would have required restructuring of every defined benefit integrated plan. To eliminate that massive plan revision and still get the congressional objective, TEFRA deals only with those plans which were congressionally determined to be top heavy (i.e., one in which more than 60% of the benefits go to the key employees). In that type of plan you could still have whatever plan formula you wanted. Congress didn't dramatically or directly change integration, they didn't directly change your plan benefit formulas, and they did not directly change your accrual rules. All they said was after you've maximized your benefits for the key employees under what normal techniques you would use in terms of plan design, if when you've finished more than 60% went to the key employees then a floor amount would have to be added. That floor amount in the defined benefit context will be a benefit of 2% per year of service not to exceed 20%; in the defined contribution context that will be a contribution of 3%. Those minimum contributions or benefits are non-integrated and there are instant accrual rules that override 411(b). You must have a floor benefit under the plan determined without regard to integration and only if the plan benefit is greater than that floor will your integrated formulas ever come into play with respect to your non-key employees. As Vince notes, this may have taken a lot of the stress off defined benefit social security integration. You may integrate as you choose so long as you provide this floor.

This leads us to whatever Congress might be doing in the near future on integration. It seems fairly clear that after this summer's spurt of pension legislation they may be reluctant to undertake additional revisions immediately. It is also relevant to note that under social security integration, there was tremendous controversy before they made the changes in TEFRA. The Rangel bill in particular caused a great deal of outcry because the social security commission isn't due to report until December of this year. There was a lot of feeling that the mere fact that the IRS had not updated their revenue rulings to reflect changes in social security, it shouldn't mean that Congress has to act now while knowing that whatever they do will be changed in the next year or so with social security. I think all of us know that there is tremendous Congressional pressure on social security. You can't keep the present benefit and tax structure and maintain a solvent system. It's equally obvious, as Don pointed out, that there is a definite correlation between social security and the private pension system. That correlation is one the Congress themselves are increasingly aware of. All the testimony this summer regarding changing the integration rules and the impact on plan costs really brought that point home. I think there will be tremendous tension as we go into social security legislation next session. Only after that is resolved will there be any possible change in the pension area. If they resolve it indirectly by proper planning of social

security, that proper planning coupled with the top heavy minimum benefit rules may totally remove any need for further statutory changes to the way in which plans are permitted to integrate with social security. The good news is that this summer, those members who are most distressed about the multiple offsets by "excessive" integration that was permitted under 71-446, finally came to realize the theoretical justification for social security integration. So, it seems that integration will be with us in at least some modified form for many years to come.

ALLAN WEAVER: We are very active in the professional corporation market, and of course, we feel the law was directed primarily toward our clients. The question I have in particular on the top heavy provisions is that TEFRA bites its own tail -- that the provision and the determination of top heaviness reflects the benefit formula and the accrual in the prior year. If you add the minimum benefit for any year in which your plan becomes top heavy the next year your determination may be that the plan is not top heavy solely because of the presence of the minimum benefit accrued from the year prior. The funding of these plans, from an actuarial point of view, may present problems with regards to cash flow, benefit adequacy, and in explaining results to the client as to why his contribution in one year is $50,000. and the next year his plan is over funded because it's no longer top heavy. It seems to be a very unworkable rule in practice and I hope we get some relief that is consistent with the spirit of the law but at least is much more workable than the literal interpretation of it.

ELAINE WORDEN: The top heavy provisions, in our view, may cause some complexity if plans do, in fact, go in and out of top heavy status. That point was brought up during the summer and there were some analyses done. It was felt that there would be very few plans really going in and out of top heavy status although obviously the provision of the minimum benefit would help any plan that was marginal. There was some stability rules built in which provided a 5 year drag back of distributions (a 5 year determination of who is a key employee), which will also help to build stability. It is true, notwithstanding these provisions, that some plans may move out of top heavy status after only one year, at which time the employer would be free to amend his plan subject to the normal 411 rules regarding who can change vesting schedules and who cannot. In no event, however, would the mere fact that an employer who is subsequently not top heavy negate the accrual on behalf of those participants who were enrolled in the plan during the top heavy period.

ALLAN WEAVER: What the problem is, of course, is you'd have to fund that accrual adequately in the year it is incurred. A fully accrued benefit at age 25 is fairly expensive.

DONALD S. GRUBBS, JR.: You can use, of course, a projected benefit cost method. Nothing forces you to switch back and forth every year. Unless the company had a lot of tax considerations, I would think that the cost of making amendments and the additional legal and actuarial fees would hardly justify jumping back and forth. I would stick with the top heavy rules unless there was a lot at stake.

ALLAN WEAVER: The law hits the small plans. Not necessarily the professional corporations or the abusers, but the small employers, and it is those people that may have struggled to put in a 10% flat plan. Certainly no one would say that there was any attempt to be top heavy when it was created. It just simply is top heavy by definition. Assume there are only four people in the plan. One person earns $50,000. and the other three earn $10,000. and are young. They don't have as large of an accrual. It's very unadministrable in my opinion. I think it has to change. I will go on record as having said that.

DONALD S. GRUBBS, JR.: I'm not an advocate of these TEFRA changes, but your comments highlight two other important aspects of integration in the larger sense. If we're really going to build a system which combines the private plan and social security to provide a flow of income that replaces the income before retirement, there are two other parts of benefit design that have to be integrated. The first is coverage. Social security covers all workers. We only truly have integrated plans when we get universal coverage of private plans. Secondly, there's the matter of vesting. Many people do not have a flow of income that is even because of lack of vesting. The need for rapid vesting is apparent in all plans, and only if we have full and immediate vesting in all plans will the private plan provide a flow of income, which together with social security, will replace the pre-retirement income.

CAROL W. PROFFER: Without addressing the income adequacy question, I'd point out that though it may seem as though TEFRA has a very large impact on small plans, in part that stems naturally from the Congressional intent this summer, which was to say that sooner or later somewhere we've got to draw an arbitrary line and insure that no one gets a tax subsidy unless so much goes to the rank and file. The line they drew was 40%. If you have a plan with more than 60% going to the key employees, you must provide this benefit to rank and file employees. Obviously, the more employees that you have, the greater the chance that you will not be top heavy, arguably because you are then effectuating the tax policy justifying your expenditure. If you are smaller, the corresponding argument can be made without the minimum benefit, you're getting a tax expenditure without effectuating the Congressional policy.

VINCENT AMOROSO: Let me discuss a question which was precipitated by the discussion between Mr. Grubbs and Mr. Weaver. In consideration of the minimum funding requirements, once a plan goes into top heaviness, the issue is whether the plan provisions giving rise to the minimum benefit will remain in effect, or whether it's an actuarial assumption as to the plan's utimately not being top heavy and therefore can drop the minimum benefit. From a minimum funding requirement, would that be a plan provision or an assumption under current regulatory and funding requirements?

DONALD S. GRUBBS, JR.: The top heavy provisions are required to be in all plans, not merely top heavy plans. They have to be in all plans on a contingent basis. In any year in which your plan becomes top heavy they automatically go into affect.

VINCENT AMOROSO: So that argues an assumption.

DONALD S. GRUBBS, JR.: Apart from the possibility that IRS may issue a regulation saying that certain plans don't have to have them, presumably an employer with 100,000 employees must have this provision in the plan and the actuary must make his best estimate as to whether the provisions will ever apply.

CAROL W. PROFFER: The recent legislation looked at several areas of the integration requirements. However, they did not address three of the specific problems which Don raised: (1) the complexity of the current integration requirements, (2) the non-recognition of changes, particularly the 1977 amendments, and (3) the inequities which exist in the way the current integration requirements apply, particularly for defined benefit plans. Do you see any particular discussions of changes to address those problems?

ELAINE WORDEN: If you are trying to get the theoretically allowable integration formulas, I don't see how one can do that in a very simple method. I think that was made abundantly clear at the Rangel hearings where the pension industry defended 71-446 and all those complicated formulas. As to whether or not the Congress would be interested in statutorily compelling periodic review by the Service, that's something that was considered. It was not felt appropriate that 401(l) changes obviously will need or require some kind of revision and update. Other than that, no decision was made to touch the defined benefit plans, so there will be no required updating of those provisions as of now. What that means, in practical effect, is that because of the general support for integration as it is now, let's not increase plan costs by changing it. The IRS has a tremendous administrative burden whenever it attempts to change those procedures or to update them to reflect social security changes. That pressure has meant that since 71-446 the IRS, though it has attempted several times to begin such a revision, has never been able to get through public comment, through the Treasury, and actually to implement such changes. I suspect those pressures will remain with us.

WILLIAM HSIAO: I'd like to comment first on Don's point and then raise a question. Don was trying to measure the adequacy of the integration formula by agreeing with the Chang paper that any pension along with social security should try to replace roughly 80% of the pre-retirement pay. That approach avoids one important element in our whole savings pattern in the United States. Namely, we are saving through social security, through private pensions and through personal savings to replace our pre-retirement pay. There has been theoretical justification since the 1930's in the tax law legislation to leave a large proportion of room for the well to do people, to save on their own for retirement, and not to fill in completely by private pensions or social security. By the adequacy rule that you propose, Don, that means that you are treating the rich and the poor alike and you are avoiding this third element of personal savings. In that context I'd like to pose a question to both Elaine and Don. If you're taking that third element into account, how will you change the adequacy rule or the design of an integration formula? The second part of my question to Elaine is: Has the U.S. Congress taken that into account in the recent debate?

DONALD S. GRUBBS, JR.: I think you raised a good point. What happened to the third leg of the retirement stool? There is a lot of evidence that for lower paid people there is virtually no third leg. That substantial savings is only done by the higher paid. You suggest perhaps that maybe the goal should be modified at 80% for lower paid people and reduced for higher paid people (i.e. we should discriminate against the higher paid in a sense expecting them to do more on their own). I think there is some rationale for that. Of course, as a practical matter, even though we adopt plans that follow the 80% rule, it would be rare indeed when those two sources would result in the 80% because (1) very few people spend a 40 year career with the same employer, (2) we have the coverage problems, (3) the lack of vesting problem and (4) even with respect to the people who have full coverage who change jobs the inflation problem with respect to the vested pension they earned at an earlier rate of pay.

ELAINE WORDEN: During the Rangel hearings there was a significant amount of testimony that the Rangel Bill would create reverse discrimination and force the employer to provide more to the lower paid employees than for the highly paid employees. There was tremendous controversy on that, and an attempt to make that the issue and to deal solely with retirement income adequacy. However, that was not the main concern of the Congress. Congress was concerned about the extent of tax expenditures and the evidence that very little of that expenditure was really being provided for the rank and file. They dismissed, if you will, the arguments about retirement income security. They didn't get into an analysis. They just said "we're either going to do something to eliminate the pension tax subsidy or to at least insure that we're getting something for the money that we spend". Mr. Rangel clearly analogized these two direct spending provisions. They think there's no way in the world that we would ever, especially in these economic times, structure a spending program that gives $9. out of every $10. to a more affluent individual or a prohibited group member.

VINCENT AMBOROSO: Both ERISA and TEFRA address Mr. Hsiao's point indirectly, if not directly, through the so called 415 maximum limits. Whereas there is the general uniform relationship rule in the discrimination standard, there is an overriding rule that plans cannot provide more than a certain amount of benefits so that Congress originally in 1974 and again in 1982 reaffirmed their efficient use of tax dollars.

DONALD S. GRUBBS, JR.: I proposed some ideas about what to do under social security if the retirement age is increased from 65 to 68. What do you think should be done with private pension plans either in plan design or with respect to the law that now requires a normal retirement age of 65 or age 65 and 10 years of participation under ERISA, or with respect to the integration rules? What should we do when social security retirement goes to age 68?

LYND BLATCHFORD: Don and I are generally in agreement. I feel, as do some of the vocal members of my corporation, that we should look towards advancing the age to 68, not only under social security but under ERISA and TEFRA. Longevity has changed substantially since social security

was implemented and we should amend all our laws so that they are consistent and integrate that way.

ELAINE WORDEN: Let me point out that TEFRA made one step in that direction by permitting an increase in the dollar limitations for any benefits which commence after 65.

DONALD S. GRUBBS, JR.: Would you concur with my thought that substantial cost reductions would be achieved if we made a change from 65 to 68 in private plans? And would you pocket the difference or use it to improve benefits?

LYND BLATCHFORD: Our position would be to use that money to provide some sort of inflation protection through indexed benefits.

RALPH BRASKETT: The obvious solution is to raise all the retirement ages simultaneously. Otherwise you get a complex nightmare that will make pension plans even harder to understand and communicate to employees. As a practitioner working primarily with small clients who are going to have to meet the top heavy requirements through plan revision or until Congress changes the law again, my clients will probably pocket the difference or use it to cover their group insurance costs which are escalating rapidly.

ELAINE WORDEN: You indicated that your clients will probably be perpetually top heavy. Do you not have very many that are marginal?

RALPH BRASKETT: Yes, I've got some. Even when the so called disparity between HR-10 plans and top heavy plans are eliminated in 1984, some of my law firm clients will still be top heavy. At least when we try to combine the partners' plans and the employee plans under Revenue Ruling 81-202.

ELAINE WORDEN: Would you conclude that the majority of your plans are on the line?

RALPH BRASKETT: It depends on what the regulations state. Obviously the clients that I have that are now top heavy would manipulate the regulations and lobby in Washington D.C. for the most favorable interpretation of the top heavy regulations.

CAROL W. PROFFER: One of the arguments being made for not increasing the retirement age is the fact that we are increasing morbidity rather than the longevity of people. People in poor health are living longer rather than people who are in good health. I don't know that I particularly support that proposal, but it would seem to me if private pension plans increase their retirement age to 68 assuming social security makes such a change, that perhaps some of that additional savings should be utilized for their benefit alternatives such as increased disability, etc.

JOSH BANK: What I seem to be hearing is that different retirement ages would be too complicated. It would cost too much to supply the same benefits. People are living longer and medical advances are such that

you can enjoy life longer. I don't want my life span to be 180 years and have to work until I'm 166 because it's predefined that I get exactly 14 years of retirement. I want to enjoy my retirement. That's from a personal point of view and I think we can handle whatever confusion comes out of it.

CAROL W. PROFFER: Essentially we should have a more flexible lifestyle than we have right now. Retirement should not be confined to 65.

DICK HESTER: Before we start worrying about what we're going to do when social security's normal retirement age is raised to 68, we should consider first how we're going to amend the Constitution. If anyone in this room believes that as long as Congress is up for election every two years they are actually going to change that normal retirement age to 68, I'm in the wrong place.

ALAN BERGER: How do you reconcile an increase in retirement age with 10.1% unemployment?

DONALD S. GRUBBS, JR.: That is slightly off the immediate topic but it is an important question when we try to project the social security problems. We need to ask not only what is a suitable retirement age in terms of financing social security but how many workers will society need in the future? The period in which those projected increases are scheduled under some of the proposals are different: some advocate starting the increases in 1990, some indicate starting them in the year 2000, the absolutely right number is 1995 because I become 65 in 1994. But it's at a time when the proportion of the population in the active working group would otherwise be shrinking. If we need the same proportion of the population to manufacture and produce the goods and service that society needs, we'll need more workers and that will fit in. Whether, on the other hand, improved productivity will mean that we need the lower proportion of people to produce all of the goods and services the society needs, that's the kind of projection I'm not able to make.

DONALD S. GRUBBS, JR.: Should the basic principle of integration be based upon trying to design needs oriented pensions or should it be designed on discrimination as the current law is? Would anyone care to address that question?

LYND BLATCHFORD: I'm not going to answer that question precisely the way it was phrased. Looking at TEFRA and how it came into being and looking at how we are addressing the question of integration, I think it's time that this country adopted a national retirement policy, and I am responding to your question in that fashion. What is it that this country wants as a policy? Should we play games as we did with TEFRA, and look at the tax situation, or are we going to sit down and determine what this country needs as a retirement policy? After that has been determined, we can look at how integration and taxation could be a part of this.

VINCENT AMOROSO: Part of the question should include how large a pension pot do you see. Insofar as you see an all encompassing pot, then maybe

national design makes relatively more sense than a limited pension pot that might have to be shared on a non-discriminatory basis.

DONALD S. GRUBBS, JR.: With that in mind, what do you think of my thoughts that for those that can't provide what I call the optimal pension that fills all the needs, then we limit where the cutbacks can be made.

VINCENT AMOROSO: Without getting into the details it seems to me that the present rules are not responsive to the current situation. Certainly in 1972 there were big changes as well as in 1977 and 1978. It's not at all clear to me that the benefit levels we've been discussing wouldn't fit comfortably within the current regulatory standards.

PAUL HALLIWELL: Don, I don't think your scenario addressed the defined contribution concept of integration. How would you approach that?

DONALD S. GRUBBS, JR.: I struggled with that one. I struggled with quite a variety of formulas which on a defined contribution basis try to produce the kind of benefits that you think might be adequate and they are so unpredictable. It's almost impossible to try and equate defined benefit and defined contribution plans and maybe we shouldn't try. The plans themselves are designed with an entirely different philosophy. A defined benefit plan is designed to meet benefit objectives. It makes sense to develop integration rules based upon meeting those benefit objectives. That's why I had suggested that with respect to them we don't consider (1) employee contributions (2) the disability benefits and (3) the death benefits. See if you are meeting the benefit objectives for pensions. When we come to defined contribution plans, we're not really trying to get a specific benefit, or if we are we're not apt to successfully do it. Even in these wonderful target benefit plans that I've written about, we usually miss the target substantially. I suggest that for them the idea of integrating contributions with contributions under Social Security isn't bad. I don't have much problem with the TEFRA rules at 5.4%. The practical matter is that only a small percentage of defined contribution plans are integrated.

PAUL HALLIWELL: From a philosophical point of view you would endorse the acceptability of a 5.4% pure excess plan whether the plan is top heavy or not.

DONALD S. GRUBBS, JR.: Yes.

ELAINE WORDEN: At the Rangel hearings the testimonies in regards to this or a similar integration change in a profit sharing concept was not of primary concern. People are much more concerned with the defined benefit.

WILLIAM HSIAO: I don't have an answer to Don's question, but I would like to broaden your question somewhat to make another plea. It's interesting that you're raising the question whether the pension benefit should be integrated or should there be a means test. These are primarily social policy issues. I'd like to comment that recently there was a national committee on pensions and only a few actuaries participated in that effort. The Society had some organizational representatives but most of the ana-

lytical work was done by economists. In conjunction, this past year the Department of Health and Human Services has given $1 million to an institution to study the retirement policy in the United States. There is a conference here in Washington on Thursday and Friday on retirement policy. Very few, if any, actuaries are to be invited to participate. What I'm saying is that I think it behooves the Society of Actuaries to look at the larger picture rather than looking at 415(c) or 77-21. Some of us should look at the larger picture as you pose the question.

DONALD S. GRUBBS, JR.: Do all these rules make any difference for most plans? I'm talking about the 100% offset and we now have a rule of 83-1/3% offset. I have very few clients who have more than a 50% offset now. After all, employees don't like more than a 50% offset since they figure they've paid for half of that benefit. Does it really matter what the rule reads?

LYND BLATCHFORD: The answer is yes and no. We have a rather interesting mixture of clients. We have a large number of small clients and we have a small number of large clients. For the small clients the rules matter. For all the clients, the recordkeeping is my concern. Whether it has some appropriate social objectives, TEFRA is an administrative nightmare to the extent that we are diverting monies to the administrators or those providing services without providing the monies to people to whom they are intended. I think these rules do matter, but not in the sense that you ask. They matter in the sense that it is providing extra administrative costs.

DONALD S. GRUBBS, JR.: In my hope of getting at rational benefits by going to the 80%/100% rule, you think it would never accomplish much for most plans. It's a small minority that will really opt for that.

LYND BLATCHFORD: I concur with what you're saying. We do have one plan where we attempted to achieve a formula such as you have illustrated, and we used a rather interesting approach. We thought we were pretty clever when we did it. But, generally speaking I think there are definite financial limits as to the ability to achieve this type of thing.

JOSH BANK: One problem in having a formula such as 80%/100% is that employees may not think of it favorably as having 100% of their social security taken out. Maybe we should investigate the possibility of stating the plan benefits something like "when you retire we will try to provide about 80% of what you were making before you retired" and not tell them exactly what formula we're going to use;not knowing what formula we are going to use until we actually get there. If that's what we're trying to do, why don't we tell them that.

CAROL W. PROFFER: Do you think that will satisfy the Department of Labor's Summary Plan Description requirements?

JOSH BANK: That was the approach that we used. Essentially, we emphasized the positive rather than the negative; rather than saying we're taking away, we're adding.

DONALD S. GRUBBS, JR.: There is always a difficult communication job. I remember stressing at one instance how your plan plus half of your social security provides these benefit levels and an employee said "you mean the more I earn under social security the more they take away from my company pension!"

RALPH BRASKETT: That's one of the problems of offset plans. In response to Don's question, it matters because most people in our society have multiple jobs and I think the model you presented and the one that's in the paper written by the Johnson & Higgins group, walks away from the fact that many people in our society, which is increasingly mobile, have six, eight, ten or twelve jobs. Don and I are good examples of that, and it is probably similar for other actuaries. The integration rules really matter. One of the things I'm curious about is why the Congress in its infinite wisdom is not going to encourage my clients to set up integrated target plans where they can use the defined benefit integration rules rather than the scaled down simple profit sharing plan rules. I never understood why they only cut back defined contribution plans.

ELAINE WORDEN: You didn't understand why they did not cut back defined benefit plan integration?

RALPH BRASKETT: They only cut back defined contribution plans. There was no cut back in integration. There never was any statutory interference with integration before, and there is some actuarial baling wire that holds 71-446 together. It's probably not valid anymore but there was an attempt at validity, as I remember from what Vince's paper indicates.

ELAINE WORDEN: I don't think anyone disputes the validity of those assumptions in 71-446 terms or facts. I think Congress was concerned, because of the social security changes, that those facts were no longer relevant. The administration has been unable to change it, whereas Mr. Rangel proposed radical changes affecting both defined contribution and defined benefit changes. As they indicated at the hearing there was not a tremendous outcry about the defined contribution changes. Even a member could understand that if the tax rate is 5.4%, then how can you justify 7%. The defined benefit integration, however, was a much more complicated subject and where the industry rose up in mass because the solution was so extremely radical that coupled with the pending social security reform that may be upon us led the member to say, with the Treasury's full concurrance, that it was more appropriate in the defined benefit context to hold off. Without the top heavy rules you got at it indirectly. Because of Mr. Rangel's interest in helping the rank and file, I would say that there is nothing to stop future changes to defined benefit integration. However, as Vince noted, the worst abuse that disturbed the members was that through various means including "excessive integration" the rank and file were not getting benefits. That concern is somewhat alleviated by this legislation because of the top heavy concept where you get a non-integrated benefit, and in a mobile workforce where you get multiple minimum benefits. That may remove some of pressure.

RALPH BRASKETT: Was a study done to indicate that only small employers have excessive integration?

ELAINE WORDEN: There was none. There was some demonstrated "apparent abuses". You can look at the multiple offset problem. You can talk about plans that have a unit benefit with a full offset. A lot of the members felt that these things were not appropriate.

RALPH BRASKETT: Why was this only lobbied against small business? Basically the top heavy requirements hit two groups of people. One I think will continue to evade the regulations, the so called associated service groups, although maybe tightening up of the control group legislation will help that. I have faith in them because they did a pretty good job with ERISA. The other is the medium and small company which is owned by its employees. They were singled out for special attention, while larger companies were not.

ELAINE WORDEN: The focus this summer was on getting benefits to the rank and file. It wasn't on a small plan/large plan basis. Integration was one of the major concerns. They ultimately did reach that problem indirectly through the minimum non-integrated benefits. There was some argument that if you were not top heavy, it follows that the rank and file are getting substantial plan benefits, and the employer's plan design has already accomplished the Congressional purpose in getting some benefits to the rank and file. If the plan is top heavy, then the minimum non-integrated benefit will apply. However, there's obviously some argument that in a non-top heavy plan which may be non-top heavy merely because of the volume of participants, there could still be integration abuses similar to those which Congress was concerned about and there is some argument that they may need future change. Until social security issues are resolved, I would doubt that there will be further action limited to this area.

RALPH BRASKETT: One last question. What is an integration abuse? I heard that term a number of times but have not heard any definition. I hear you using the term which means it must be local Washington jargon.

ELAINE WORDEN: I try to say alleged or perceived integration abuse. The concern this summer was on multiple offsets, cumulative offsets, the hard offset where you had a unit benefit accrual with a full social security offset. Those were perceived to be abusive in that it allowed any one employer "excessive" integration.

RALPH BRASKETT: That's what an integration abuse is?

WAYNE DYDO: What is the status of the debate concerning the appropriateness of the CPI index as an inflation adjustor for post-retirement benefits? Some people maintain that social security is over indexed because of the way that the CPI is determined.

DONALD S. GRUBBS, JR.: There are those who would like to reduce CPI indexing. Incidentally, the American Academy of Actuaries has apparently endorsed cutting back full CPI indexing in both news releases and in a kit on social security which they have released to local actuarial clubs for use. I think this is entirely improper for the Academy to represent as a viewpoint of the Academy, viewpoints which are not shared by many of its members without any indication that some of us have very strong

differences with that. Pensions which are not fully indexed for cost of living are in fact decreasing pensions. The CPI is not a perfect index. Particularly, the housing component has been a difficult thing which caused the index to rise more rapidly than the cost of living in years when interest rates have gone up and more recently has caused the CPI to rise less rapidly than the true cost of living. That's a problem which the administration has decided to solve by correcting the housing component. Within another year or two that problem will be behind us. Some would switch to a wage index. Those who advocate a wage index are really advocating the lesser of wage index or price index. The rationale behind that is "why should the retirees do better than the active workers". The other side of the coin is "why should the active workers do better than the retirees". Those who feel that retirees should share when wages are going up more slowly than cost of living should look at the other side of coin. For many years throughout the history of this country, wages have gone up substantially faster than the CPI. Those who retired 15 years ago have not shared with the increase in productivity and increase in standard of living that active people were having through wage increases even if they were fully indexed for the CPI. Therefore, the lesser of the two is not a fair approach. Secondly, to say, well why don't we wage index indefinitely into the future, if the future is anything like the past that would be far more expensive than CPI indexing. The system can't afford it. There may be some merit to that approach, but I don't think the system can afford it.

ELAINE WORDEN: TEFRA increased the pressure on whatever formulas they used to adjust social security benefits because effective in 1986 the 415 limits applicable to private plans will be adjusted for cost of living in the same formula as then in effect for social security benefit increases.

CAROL W. PROFFER: I concur with Don's approach that reducing the amount of increase to future retirees to the lesser of the increase in wages and the increase in the Consumer Price Index is probably inequitable for those people for several reasons besides the one he has stated. One of the reasons that we have such an affluent existence is because of the lesser existence of people who are now retired. Consequently, I don't see why future increases in benefits should be cut back to the lesser of wages or the lesser of the CPI. I do feel that the CPI needs to be adjusted for the housing component and the fact that that resolution will be made very shortly does seem to resolve much of the concern about the CPI. There is, however, substantial support for changing the basis of increasing retiree benefits. And because we don't know what's coming out of the Commission on Social Security until some time in November, we can't actually see what they're going to propose in this particular area.

JOSH BANK: There's going to be a lot of pressure over the next year or so, if the retired group can apply pressure, to have the basis changed from CPI to some other retired CPI. Interest rates are now coming down and if they keep going down they're going to drag the CPI down to under zero. The things retirees are buying may still be going up at 5% or 10%. It's just like when they were getting a big bonus when interest rates were going up since housing plays such a large part of it.

VINCENT AMOROSO: There is a very good reason to have the index be the lesser of the change in wages or change in CPI. If in typical times wages are increasing faster than the cost index, then those might be called typical or good, or non adverse time. During those times retirees benefits could increase with the cost of living. During times of adversity, why should the retirees be skating ahead of workers who are perhaps not doing their first choice in working an 8 to 5 job. In my mind it seems unfair the other way. In good times certainly they should have their benefits increased in accordance with change in CPI, but in bad times they should share some of the adversity.

CAROL W. PROFFER: Do you not think they shared some of the adversity in prior years?

VINCENT AMOROSO: You always have transitional problems.

PAUL HALLIWELL: It always amazes me that the government seems willing to spend $2. to collect $1. One of the principal reasons for TEFRA was to raise revenue. I should not kick the dog that's going to keep me company, but I'll make a lot of money off of TEFRA and many of the people here will. Money that's going to be deductible for our clients. I just wonder if there's going to be a net revenue gain out of the pension aspect of TEFRA or if there's any estimate as to how much this is going to cost the government in taxes.

ELAINE WORDEN: The revenue estimates indicated that over the three year period TEFRA pension provisions would gain about $1 billion. They took into consideration some of the administrative problems. I'm not a revenue estimator or an economist, but I'm sure our staff that does those estimates did take into consideration the costs. I'm sure the other thing they took into consideration is the diminishing amount of corporate taxes anyway. The administrative fees are deductible in a corporate level but if the corporation is not paying taxes then there's no net loss to the government. Generally, our estimate and the Treasury's estimate comes out pretty close, at least on a projected basis from the material and data we have on hand.

DONALD S. GRUBBS, JR.: Elaine, I would say in response that they had a very tough job. They didn't have the data necessary to make that determination. There is no way with the data available that either the joint committee or the Treasury could make that kind of determination. In contrast to the kind of studies that we did in preparation for ERISA, where we made an effort which took some time, they didn't have time to gather the data and do the kind of calculations and study that were needed to determine costs. I don't think anyone knows what the cost effect is.

RALPH BRASKETT: In 1984 when plans are amended for TEFRA minimum benefit, will we be permitted to use a year over year formula to meet the 20%? Do you have to give a participant 20% of his average 5 or 10 years of service with the firm regardless of his age?

ELAINE WORDEN: The minimum benefit rule is an override to the normal accrual rules of 411(b). You accrue the benefit for the year in which it's top heavy.