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LIMITED PERIOD EARLY RETIREMENT INCENTIVE PROGRAMS

Moderator: WILLIAM J. SOHN. Panelists: LAMBERT R. BUTZEN, MYRON HOCHHEISER, CHARLES C. HABLISTON. Recorder: RICHARD C. FULLJAMES*

MR. WILLIAM SOHN: This session is on Early Retirement Incentive Programs also known as open windows, golden handshakes or golden parachutes.

We have three panelists today who will bring three different viewpoints to bear on the problem. On my left is Charlie Habliston who is a consultant for the Wyatt Company in Washington, D.C. Charlie just completed work on the implementation of a window for a medium-sized airline. This is a company with about 100 employees who were eligible for the window, of whom 44 were people that the company had targeted as people they would have liked to retire. It's an interesting case, a small case where the intentions of management and the people involved were much more obvious than they might have been in a larger company. Charlie is going to give us a general overview or definition of the subject and the problems related to implementing a window, as well as talking about his involvement with the airline case.

Myron Hochheiser, on my right, is Director of Actuarial Research for the Actuarial Benefits and Compensation Consulting Group at Coopers & Lybrand in New York City. He has served on the Principles and Practices Committee for the Academy. In August, the Financial Accounting Standards Board, as you probably know, issued its Standard No. 74 dealing with the proper accounting for early retirement benefits. Myron is going to address the conceptual and the measurement problems that the Standard has created for actuaries and consultants.

Last, but very definitely not least, on my left is Bert Butzen, Benefits Manager for Beatrice Foods Co. in Chicago. Beatrice is a large corporation with over 60,000 employees domestically. They have just completed a window program that serves as a good contrast to the one Charlie will talk about, from the sheer size of the program and the diversity of the types of companies under the Beatrice umbrella. Bert has a video tape that was part of the communication package that was used by Beatrice in introducing the program to its managers. I think that after seeing it, it will become clear why good communication programs are such a critical part of a successful window.

I am now going to turn the microphone over to Charlie Habliston.

MR. CHARLES HABLISTON: Thank you, Bill. My presentation this afternoon is modeled after an actual early retirement incentive plan that was established this summer for a medium-sized airline that was large enough to

* Mr. Butzen, not a member of the Society, is Manager, Employee Benefits/ International Benefits Programs of Beatrice Foods Co.

need an early retirement incentive plan, but too small to design and implement the program without outside help. The areas for discussion include:

(1) The purpose of an early retirement incentive plan,
(2) The basic elements of the plan,
(3) The benefits offered,
(4) Communication to employees of the early retirement incentive plan,
(5) The cost of the plan,
(6) Disadvantages of the plan and
(7) The cost of consulting and preparation aspects of the plan.

Purpose

The purposes of the early retirement incentive plan can be equated to the employer's objectives. In the airline's case they were as follows:

(1) To eliminate obsolete jobs,
(2) To terminate less productive employees,
(3) To ease older employees into retirement,
(4) To open promotional channels for younger employees,
(5) To improve the cash flow situation,
(6) To avoid lay-offs or pay-cuts, and, finally,
(7) To cut costs and improve operating efficiency.

Basic elements

The basic elements of the early retirement incentive plan were as follows:

(a) Encouragement of early retirement,
(b) Availability for a limited period of time,
(c) Availability to a specific group of employees, and
(d) Voluntary participation.

The incentive provided must be large enough to make early retirement affordable when added to the employee's other benefits at retirement.

The encouragement of early retirement

As the plan was established, prior to the window, there was a heavily subsidized early retirement benefit in the amount of 3% reduction per year to age 60 applied to the accrued benefit and then from age 59 down to 55 it was reduced by 6% per year. In addition to the subsidized early retirement benefit, cost of living increases were provided for retirement benefits with a cap of 6% per year. Nonetheless, few plan employees were inclined to retire. The airline needed a more attractive incentive to encourage early retirement.

The limited period of time

Generally this period will run between two and six months. The airline chose three months for its time frame. As a design consideration you do not want the time frame too short. The employees need time to make a prudent decision concerning retirement and this cannot be made overnight. If the time frame is too short, too few employees may elect to participate in the early retirement incentive plan. On the other side of the coin, you do not want the time frame to be too long. For one reason, the company will not realize the immediate cash flow savings. Also, more employees than originally anticipated may elect to participate in the early retirement incentive plan. The general two to six month time period provides the time necessary for the administration and communication of the plan to the selected group of employees.

Specific group

Selected groups of employees are a definitely defined class. In the airline's case, it was those eligible for early retirement who, under the plan provisions, were those between ages 55 and 65. This window corresponded to 107 employees who were currently eligible. Forty-four of the 107 were a target group according to management. Of these 44, 20 were to be replaced. Since the benefits were provided through the qualified pension plan, potential IRS discrimination problems were avoided.

Voluntary participation

The program was strictly voluntary in nature. No employee was forced or even encouraged to retire. The decision to participate in the window was an individual choice.

The success of the plan

Out of 107 people that were in the window, 53 accepted. Forty out of the 44 ear-marked by management elected to accept early retirement. It was felt that both the employer and the employees knew who the targeted group were.

The benefits offered through the program

Among the benefits offered under the window were elimination of actuarial reduction for the accrued benefits payable before age 65, a Social Security supplement to age 62, and a severance pay benefit, the amount of which was 1-1/2 weeks pay times the number of years of credited service. Group life and health benefits to age 65 were also offered, as well as travel benefits to age 65. In addition, a level income option that was actuarially equivalent to the cost of living benefit at retirement was provided.

The communication of the plan to the employees

Personalized forms were distributed to the employees, printed on the Company letterhead and signed by the President of the Company. Also, a presentation of this program was made to the employees who were part

of this window group. In addition, retirement counseling was made available for the eligible employees in the window.

The cost of the plan

The cost of the plan can be summarized as follows:

1. The present value of the additional benefits provided, plus
2. The administrative, legal and actuarial fees involved, plus
3. The actuarial losses resulting from the introduction of the program, plus
4. The present value of the replacement's pay and fringe benefits, plus
5. The training and relocation cost of the replacements, minus
6. The present value of the pay and fringe benefits for retirees who elected to participate in the window, plus or minus
7. Some intangible costs such as the effect on morale and unclogging of promotional channels.

Overall this resulted in a net savings for the Company.

Disadvantages

Disadvantages of an early retirement incentive program are as follows:

1. Valuable employees may leave and subsequently work for a competitor.
2. A large reduction in a workforce in a particular unit may result due to the age and service conditions.
3. Identifying exactly who will leave the company and subsequently finding suitable replacements.
4. Finally, more employees than anticipated may elect to participate in the window which will tend to make the cost of the program rise.

The consulting and preparation aspect

We prepared employee data lists of possible eligible groups and the near-misses (*i.e.*, those people who were within a few months of the age conditions). These lists were presented to the client to give him an idea of the size and nature of the group. A list of benefits was provided for each eligible individual. An additional list was given to the client showing the cost of the plan and the savings realized per individual. Preparation of the communication materials was provided (*e.g.*, employee benefit statements showing benefits provided under the window and personalized election forms). In addition, plan amendments to the qualified pension plan were drafted and, finally, the FASB 74 calculations were developed for the accountants to recognize the expense of the early retirement incentive program in the year of occurrence.

Summary

In conclusion, the early retirement incentive program of this airline was a success for the following reasons:

1. Very attractive benefits were provided,
2. A positive and personalized presentation of the program was made to the employees,
3. A three month time period during which the window was available,
4. And, finally, 91% of the targeted group accepted the retirement plan.

Finally, I have some hand-outs that will be available at the end of our panel discussion that will show the type of listings that we prepared and the election forms that were made available to the employees to decide whether or not they wanted to participate in the plan.

MR. SOHN: Thanks, Charlie.

Myron Hochheiser will now tell us about the accounting problems.

MR. MYRON HOCHHEISER: I would like to concentrate on simplifying what SFAS 74 is calling for in a manner that clears up some misconceptions about it. I'm not going to get esoteric here because that would be boring to everyone including myself. What I will do is run through a very simple numerical example on the basis of which we can actually see what many actuaries think that the Accounting Standard is calling for, in contrast, I'm sorry to say, with what the Accounting Standard actually does call for. FASB requirements for accounting for a window period, as have already been stated, are contained in this so called Statement of Financial Accounting Standards No. 74, effective July 1, 1983. For those of you who have been involved with a window period situation that ended before July 1, 1983, the first fact to get out of this meeting is: do not think you're home free. As we'll be seeing later, some auditors have felt that the contents of this Standard have really been in place all along and you may still have to apply it. Basically, the Accounting Standard calls for only two things.

(1) It calls for an expense for special additional benefits offered, whether or not through a plan, including the act of having to take expected future payments into a present value calculation. There have not been many conceptual problems with this first of two requirements.

(2) The second requirement is really what my segment of this session is all about. Namely, a positive or negative expense (actually negative expense is income, but we'll call it an expense) reflecting how the window period has impacted upon previous assumptions under employee benefit plans. That quantification is an actuarial loss or gain type of item.

That loss or gain item is what we'll talk about primarily because that's where there have been a lot of difficulties. Let's restrict ourselves

to a pension plan setting to focus in on the difficulties, and let us consider the following facts relating to the "window period segment." The term defines itself - it is the portion of the plan related to the employees who took advantage of the window period offer.

If you want to keep up with this, I'm going to hit you with the bare minimum of numbers. They're going to be easy numbers with a lot of zeros so I can read them aloud easily myself. First of all, let's say that the accrued actuarial liability attributable to the window period segment before the actual window period event is a million dollars, an easy number. How to make this attribution is a long standing problem (under paragraph 31 of APB 8). I'm sorry, but I'm not going to solve that here because I don't personally believe that there is a specific unique solution. I think it's a badly written paragraph and it needs explanation. SFAS 74 does not help explain that. For example, if you're using an aggregate funding method, what does actuarial accrued liability for a segment mean?

The second number to write down is a number related to the value of assets. Here, it is called "previously accrued expenses." In fact, for those of you who have read this Standard, I'm going to ignore a certain mandate in it because I don't know what it means. That's the mandate to set aside previous investment gains or losses. I don't know how to do that, so previously accrued expenses for our purposes will simply be plan assets used for expensing. Now, plan assets used for expensing are the same as plan assets used for funding - the actuarial value of assets, if you will - plus any balance sheet liability minus any balance sheet assets. But again, I'm only talking about the number that somehow or other is determined to be attributable to the window period segment. Call it $800,000, yielding a $200,000 underfunding. Again, how to make this asset attribution is a long standing problem. The third number I'm going to give you is the revised actuarial liability attributable to the window period segment. That is, after the window period event. There's no problem calculating this amount under any actuarial cost method as we're now dealing with terminated people. It's simply the present value of their benefits. Let's say this amount is $1,050,000, implying an actuarial loss of $50,000.

Now, how do you deal with these facts? One million dollars is the liability before the event which becomes $1,050,000 after the event, resulting in a $50,000 loss. In the meantime, you have assets standing behind all this in the amount of $800,000. Many actuaries would use a termination accounting or full immediate settlement approach and would advise their clients to expense what they need minus what they have. That is, $1,050,000 minus $800,000 which equals $250,000. This approach in terms of an analogous situation of a plant closing was well and ably described in an article appearing in the November 1980 Financial Executive by Lawrence Best of the SEC and Paul Gewirtz of TPF&C. The expected disclaimer appears in the article but there is, nevertheless, reason to believe that the SEC agrees with this accounting view. Note that the especially difficult item, the previous accrued actuarial liability attributable to this window period segment, does not even enter into the calculation. The difference is between $800,000 and $1,050,000, ignoring that million dollar figure which is in between the two.

There's one slight problem. FASB disagrees. FASB agrees that a termination accounting approach should be used. There's no disagreement on that score. The issue is what the approach should be applied to. The $250,000 expense I just described applies the termination accounting approach to the whole of the window period segment. FASB believes the approach should be applied only to $50,000, the actuarial loss. The other $200,000, the previous unfunded actuarial liability, although admittedly attributable to the window period segment, is nevertheless not attributable to the window period event. The $200,000 arose from on-going operations of the plan. Therefore, the termination accounting approach is not relevant to it. That is what's contained in SFAS 74 with a slight wrinkle which I'm going to describe. Keep in mind that even though SEC has stewardship over FASB it has as yet not chosen to overrule FASB and I would suspect it will not. It very rarely does, if ever.

In the example described, you have the approach used by many actuaries of an immediate booking of $250,000 versus what FASB says is only $50,000.

There are other wrinkles. For example, suppose the attributable revised actuarial liability was $950,000, instead of $1,050,000, i.e., a $50,000 actuarial gain instead of a $50,000 actuarial loss. The Best-Gewirtz (and possibly SEC) approach would call for an expense of $950,000 minus $800,000 or $150,000. Now, based on what I said before, you might think that FASB would call for an expense of minus $50,000 as an income item thus leaving intact the $200,000 unfunded item for future on-going type expensing, right? Wrong! Here FASB reasons that the $50,000 is part of the $200,000. How can you take back into income a portion of something that was never expensed in the first place? Remember, in the other case the $50,000 loss was in the nature of being supplementary to the $200,000 rather than part of it. FASB's conclusion here is to do nothing with the actuarial gain, but to expense $200,000 minus $50,000 or $150,000 as part of the on-going operation of the plan, in accordance with the amortization schedule you have set up.

Suppose we had a $200,000 overfunding instead of an underfunding; i.e., suppose the attributable assets amounted to $1,200,000 instead of $800,000. Well, in the case of our actuarial gain where the attributable actuarial liability changed from $1,000,000 to $950,000, the Best-Gewirtz (and possibly SEC) approach would call for an expense of $950,000 minus $1,200,000 or minus $250,000. FASB's approach would be an expense of just the actuarial gain, $950,000 minus $1,000,000 or minus $50,000. Please note that here the $50,000 gain is in the nature of being supplementary to the $200,000 overfunding rather than part of it.

What about our actuarial loss case, where $1,000,000 changed to $1,050,000? The Best-Gewirtz (and possibly SEC) approach would call for an expense of $1,050,000 minus $1,200,000 or minus $150,000. There is no problem with a consistent way of calculating things: what you need, minus what you have. From everything preceeding we would expect that FASB's approach would be to ignore the $50,000 loss and to negatively expense $150,000 in the future rather than $200,000 as part of the ongoing operation of the plan, because that $50,000 is part of that $200,000. Unfortunately, only a very aggressive reading of SFAS 74 would support this inter-

pretation. The more easily supportable interpretation is to expense the $50,000 and to take back into income the whole of the $200,000 as part of the ongoing operation of the plan. So what we see here is that FASB is being conservative. When it comes to an actuarial gain, which is part of an existing underfunding, it is not (negatively, of course) expensed. But when it comes to an actuarial loss, which is part of an existing overfunding, it is expensed.

Let me remind you, throughout we've only been considering the gain or loss immediate expense requirement of the Accounting Standard, not the additional benefit immediate expense requirement. With respect to that complicated gain or loss matter, SFAS 74 allows for the item to be ignored (even if material) where its measurement would not be reliable. For example, where previously accrued expenses cannot be allocated between the window period segment and the rest of the plan.

Finally, I'd like to repeat something I hinted at in the very beginning. Can you successfully defeat the auditor's requirements for termination accounting calculations for a window period event that pre-dates the effective date of SFAS 74, July 1, 1983? I have to stress: not if the auditor claims that Paragraph 31 of APB No. 8 would require a calculation. That would then apply to any window period event that occurred after December 31, 1966.

MR. SOHN: Thank you, Myron, for shedding some light on a difficult subject.

We will wind up the panel presentations with Bert Butzen and an entirely different approach to the problem we're discussing.

MR. LAMBERT BUTZEN: In Chicago, an elderly pensioner sat on the same park bench every summer day and simply watched the people passing by. One day as he sat, resting his chin on his cane, watching the passing scene, he spotted another man, who appeared to be about his same age, crossing the street before him.

This newcomer had a jaunty air, his hat was cocked to one side, he swung his cane and stepped off and on the street curb firmly and surely.

The park bench sitter was so impressed that he intercepted the newcomer and said to him, "Pardon me, sir, but I could not help but notice your jaunty air, your confident stride, your obvious good health. What, sir, is the secret of your longevity?"

The newcomer responded, "I try not to sleep more than 6 hours a day. I have sex at least twice a day (day or night as the opportunity presents itself). I smoke 2 packs of king-size cigarettes daily and I drink at least a fifth of bourbon a day."

The park bench sitter said, "That's remarkable, and how old are you, sir?" The street crosser responded, "I'll be 26 next Sunday!"

I guess the only point to that story is that you shouldn't always draw conclusions about age and ability just from what you see.

My first experience with pensioners was in the early fifties when I worked for Montgomery Ward. At that time, Ward's didn't have a pension plan as such. Employees worked until they decided they couldn't cut it any more, or until they were terminated by the company for inefficiency. As these employees left, company management would review their personal assets, obligations, income and expenses. In the case of long service employees who could demonstrate financial need, the company would authorize pensions to be paid as then current expenses, subject to annual review and possible adjustment or termination, as subsequently might be recommended by the reviewing manager.

Ward's initiated its first formula pension plan in 1957. Among the reasons the consultants gave for companies to adopt pension plans in those days was that, "A retirement plan is a vehicle to provide for the systematic removal from the payroll of the superannuated employees." Under most plans then in effect, there were no judgments to be made. When an employee reached normal retirement age, usually 65, he or she retired. Managers didn't have to evaluate performance or make any hard decisions.

As we all know, this approach ended with the Age Discrimination in Employment Act of 1978 (ADEA) which outlawed mandatory retirement prior to age 70 (at present, but it will probably shortly be changed to prior to any specific age).

My present employer, Beatrice Foods Co., is a large multi-national foods and consumer products company. Our U.S. workforce, as Bill said, is more than 60,000 people who identify with the hundreds of products of Beatrice and its divisions and subsidiaries.

Beatrice responded to the age discrimination legislation, as did many other employers. In general, it has been and continues to be our policy that there is to be absolutely no forced retirement at any age.

As a consequence of that policy, over time we've seen a build-up of a fairly substantial number of marginally efficient employees in our workforce. Many of these employees might prefer to retire, but they continue to work because of financial insecurity, real or imagined, or for a variety of personal reasons. To encourage the retirement of marginally efficient workers and to improve the operating efficiency of our continuing workforce, we developed the Beatrice Foods Co. 1983 Voluntary Early Retirement Plan.

The important features of this Plan are:

1. A limited "open window" election period, in our case the 60 days from May 1 - June 30, 1983.

2. An eligibility "Rule of 75." That is, any combination of age plus full years of continuous service equaling 75 or more qualifies the employee for early-out. All employees 65 and over are also eligible regardless of service.

3. An accepting employee receives his or her accrued normal retirement pension without reduction for early retirement.

4. In addition to the regular plan benefit, each eligible employee with 20 or more years of continuous service receives a special bridge benefit of 25% of his or her final year's pay for the first four years of retirement or until age 62, whichever is later. This "bridge benefit," is payable to eligible employees with less than 20 years of service in the proportion of their actual service to 20 years.

5. Eligible retirees also are guaranteed availability of a comprehensive medical plan for the retired employee and his or her spouse during retirement.

The implementation stage of this early-out program involved two parts. First, each eligible employee received a communication package consisting of:

1. A letter specifying the employee's estimated unreduced monthly pension benefit if he elected to retire under the early-out plan.

2. A pre-printed retirement benefit determination form. This is a computer printed form that outlines the form and amount of optional types of monthly retirement payments available: straight life income, joint and survivor, guaranteed periods certain, and so forth. The retirement determination form also indicates the employee's earnings used in the pension calculation, his or her credited pensionable service and dates of birth and sex of the retiree and spouse. Included also is our estimate of each prospective pensioner's potential Social Security benefit as used in our pension calculation.

3. Finally, a form to permit election by the employee to participate or not to participate in the early-out plan.

The other part of the early-out program was perhaps more important to its overall success. As you know, some companies have become involved in litigation because their early retirement programs did not remain entirely voluntary and individuals who didn't want to retire were encouraged or even coerced into early retirement. Beatrice's top management was determined that this program would be entirely voluntary, that no one should either be forced to accept early retirement or, on the other hand, be discouraged from taking advantage of the program. Regional meetings were held with groups of subsidiaries' managers at which the program was explained. Managers were instructed to distribute the individual communications packages to the employees, to answer any technical questions, but to refrain from giving any advice whatsoever as to whether or not any individual should retire.

To assure the complete neutrality of the program, all implementation materials were prepared at corporate headquarters. Other than distributing

the packets and getting answers to questions about the benefits calculations and basic employee data, nothing was to be done in the field. To reinforce the importance that we placed on encouraging employees' decisions to be free of pressure, we asked all of our managers to see a short video tape that I'll share with you now.

(A short video tape was shown.)

The final part of the implementation was that each employee who elected to accept early-out subsequently received a "Retirement Confirmation File" containing:

1. A more fine-tuned benefit estimate,
2. A form for verifying the spouse's date of birth,
3. A form for electing the date of retirement payment that the employee desired, and
4. A booklet explaining Social Security.

At the time we were putting our cost estimates together, there were about 1,500 eligible employees spread among all the different profit centers and covered by many different qualified plans. We could calculate our maximum exposure, but it was difficult to estimate actual costs based on the number of employees who would accept the offer and retire. We finally decided to estimate acceptance according to age as follows:

Age 65 and over - 100%
Age 62 to 64 - 66 2/3%
Age 55 to 62 - 50%

This resulted in an estimated overall acceptance rate of 61% and an estimated cost of about $30 million if our estimated 61% acceptance level was met. There was considerable room for error in our estimate. This made us nervous, especially when the company decided to make a provision for it on the books at the end of the fiscal year before the offer was made.

The $30 million total estimated cost happened to be about 1 year's pay for all eligible participants.

Now I would like to share with you the results of our program, which I think you will find interesting. Fortunately, the final results were very close to our estimates - 54% accepted the offer with a total cost of $25.3 million.

Looking at the acceptance rates by age, we found that our estimates were pretty good under 65. However, to our surprise, hitting age 65 did not change the acceptance rate much at all. More surprising, those age 70 and over had a lower acceptance rate even though they were being offered, in effect, one year's pay to retire.

Even if our estimate of acceptance rates was accurate, we were still concerned that the distribution might be skewed towards the higher paid. This could mean that even if 61% accepted, it might represent more than

$30 million of cost. Fortunately, that was not the case. The acceptance rate reflected minimal variance by compensation.

Comparing the early-out results with our normal retirement experience during 1982, our early-out program increased retirement acceptance among employees ages 55 to 62 by 5 times, at ages 62 to 65 by 4 times, but at age 65 or over by only 2 times.

Overall, we felt that the program was successful and accomplished our objectives. Naturally we lost some employees we would have preferred to keep, but this was expected given the no pressure emphasis of our plan.

MR. JAMES COLBURN: I'd like to ask Mr. Habliston a question. In the airline case, did they expense the present value of all items other than retirement benefits such as medical and group life insurance?

MR. HABLISTON: Do you mean, were they included in the FASB calculations?

MR. COLBURN: Yes. Is the present value of all future benefits expensed in the year in which the termination window was offered?

MR. HABLISTON: Yes.

MR. COLBURN: Do they offer these same benefits, both retirement and medical benefits, on an ongoing basis anyway?

MR. HABLISTON: I believe they do not, based on the current plan provisions.

MR. ROBERT DOLAN: My question is also for Mr. Habliston. It concerns the effect of this plan on the qualified pension plan. There are two questions. First, how do you deal with the anti-cutback rule in accrued benefits when you essentially close the window? Second, for future valuations, do you make any assumptions as to subsequent windows further out in time?

MR. HABLISTON: I'll answer your second question first. We didn't make any future assumptions as to other windows being available. I'm sure it was a one time deal. We really had no idea or any basis to project that these windows would be available in the future, so we didn't incorporate any assumptions for that. I'm going to decline to answer your first question simply because I don't know the answer. If somebody out on the floor has an answer to that, I'd welcome their response.

MR. DONALD GRUBBS: I have a question for Mr. Habliston. Maybe I misunderstood what you were saying. I gathered there were 44 people you really wanted to retire and approximately 60 more that the program was offered to that you didn't want to retire?

MR. HABLISTON: Correct, there were 44 employees targeted by management, that is, 44 whom management would have liked to have seen go out under the early retirement plan.

MR. GRUBBS: How did you get a much lower response on the people you didn't want to retire? I understand that less than ¼ of them took the offer. Was it the same offer?

MR. HABLISTON: The same offer was available to all employees in the window. I think it was just a matter of good timing and good luck for the employer that they decided to go out.

MS. MARSHA BERA-MORRIS: A situation arose where a client was asking a question about a permanent window as part of the plan whereby as soon as an employee hit age, let's say 55, with 15 years of service he would automatically have 90 days to take some kind of enhanced benefit akin to a window benefit. Has anybody ever run into this? Are there any problems on any of the items discussed here that we might look out for?

MR. SOHN: The question was: Has anybody ever heard of a window that's always open at 55? This means that anyone who chose to go out at 55 might get a better benefit than somebody who chose to wait until age 56. Any opinion?

MR. JAMES WALLACE: Is there a way for an overfunded plan to beat FASB 74 expensing? Are there ways to structure the deal so that you can have an overfunding and not have to expense the entire increase of $50,000, as in the case of the examples earlier? Could a 90 day permanent window be taken out of the realm of a short period offer and made permanent by plan amendment, with the increase in cost spread over the future?

The general question is: is there a way of beating the expensing short of terminating the plan?

MR. HOCHHEISER: My guess would be that if it is a permanent offer you definitely would get out from under SFAS 74 or indeed paragraph 31 of APB 8. Yes, you would, but that's my personal opinion.

MR. WALLACE: By permanent offer, do you mean that anyone who hits 55 could retire early?

MR. HOCHHEISER: Yes. The whole purpose of immediate accounting, as opposed to amortization accounting, disappears when the offer is always open. It's then part of the ongoing nature of the plan.

MR. SOHN: I have a general question for both Charlie and Bert that hasn't been discussed. It relates to the kind of funding media that you might want to use to fund early-out programs. Companies have used their pension plans, but they have also set up non-qualified plans in top hat and possibly other situations. They have also paid benefits directly out of company assets. Would either of you like to comment on why the programs you were involved with chose to pay benefits from qualified plans rather than by or from any other media?

MR. HABLISTON: In our case the plan was not targeted for the key employees. Therefore, they felt the qualified pension plan could handle the payment of the benefits since a vehicle was already created for this purpose.

I think they really just didn't see the need for establishing a non-qualified pension plan to provide for these benefits. The severence pay benefits, however, were paid outside of the qualified plan.

MR. BUTZEN: In our case, the supplemental benefit, the bridge benefit, if you will, was part of the voluntary early-out plan which was separately qualified so all benefits were paid out of qualified plans, except, of course, the medical plan's expense which will be picked up as we go along.

MR. CHARLES WALLS: I have a question for Mr. Butzen. Was the expense of this plan net after salary savings described by Mr. Habliston?

MR. BUTZEN: No, it was not. Salary savings were not figured into that calculation. That's just the cost of the benefits.

MR. LESLIE JOHN LOHMANN: I'd appreciate it, Mr. Butzen, if you would go a little further with your last comment. It appears that you said that there were really two plans, your basic plan which continued without change, and then the window plan. If the window plan was a separate and separately qualified plan, then I am very interested in your approach to the IRS.

MR. BUTZEN: Again, perhaps this may be something unique to Beatrice because of the nature of the company and its size, when we talk about the voluntary plan being a separate supplemental plan to the underlying plan. The underlying plan may have been any one of 50 underlying plans that were in force at any one of our various subsidiaries. It was not one plan applicable to all employees. If you listened to the video tape carefully, a manager talked about the fact that it could be a profit sharing benefit. It could have been a benefit from a profit sharing plan or a benefit from any one of many qualified pension plans that were available to different groups of people.

MR. LOHMANN: My concern is with the excess cost over and above the normal pension plan cost, whatever it may have been, and the fact that this new plan definitely would not be of a permanent nature and hence, couldn't be qualified as such. If it was qualified, how did you go about doing that?

MR. BUTZEN: I'll have to have you to talk to someone else on that. If you wish, however, let me have your card and I'll have somebody get back to you.

MR. SOHN: A question in my mind is what happens when you're discussing what to put into the window and some people have heard of it before it becomes common knowledge? How do you deal with the employees who go out a month before the window opens, presumably because they didn't know a window would be available?

MR. BUTZEN: Incidentally, we religiously held to the fact that the employee only had the window period in which to make his decision. Whatever decision was made during that window period could not in any way be changed after it was made. We had some people come back after the fact both ways -

some people who opted to retire who came back and said they preferred not, they had changed their minds, and vice versa. In either case, the answer was, "Sorry, you made your decision."

MR. JOHN MUEHL: Both of the examples that were given here had eligibility rules of age 55 and up. Now ADEA protects people below that age as well. Did either of you look into the possibility of an age discrimination suit for people below age 55 who were being discriminated against because they were not included in the window?

MR. HABLISTON: On the airline case, to my knowledge we did not look below age 55.

MR. BUTZEN: If we did, I'm not aware of it.

MR. SOHN: The general impression is that the window programs weren't contemplated by Congress when it passed ERISA or other more recent tax legislation affecting pensions, or for that matter, ADEA itself. If anybody has dealt with the IRS recently on issues that might involve accrual of benefit rules or other potential technical problems, we would be interested in hearing about it. Has the IRS denied tax qualification to plans of the sort we've heard about because of technical objections that could be raised?

MR. MUEHL: To be a little more specific on the potential IRS problems, both of the examples paid unreduced benefits to age 62. Were either of the plans integrated with Social Security? And if so, did they meet Social Security integration rules for the window period benefits?

MR. HABLISTON: In the airline case, the benefit formula was an offset plan and the integration limits had to be adjusted for employees age 62 and below. The Social Security supplement that was provided bought back part of the integration percentage, but the difference that wasn't purchased through that supplement had to be reflected in the offset to the primary insurance amount.

MR. ALBERT RETTIG (of the Pension Benefit Guaranty Corporation): Last week I had a termination of one of these plans that provided 55 and 15 unreduced benefits for life. The guaranteed liability of this pension is still up in the air. I was just curious, if one of these plans should terminate with insufficient assets, what would you tell the client?

MR. SOHN: Do you feel that the PBGC would accept the risk?

MR. RETTIG: I don't know. I'm just saying that that's the top of the problem that has to be looked into. IRS has problems with the interpretation of the accrued benefits and so forth.

MR. MUEHL: I have a question for Mr. Hochheiser. He's used a term a couple of times, the window period segment. What is that?

MR. HOCHHEISER: That term refers to the people, not to whom the benefit was offered, but the people who took the benefit. Treating them analogously

to a plant that has shut down, we then applied these rules to the people who accepted the offer as a class.

MR. MUEHL: The implication in that is that this group of people retired under the window provision, but would not have retired otherwise?

MR. HOCHHEISER: That's correct.

MR. MUEHL: How do you know that?

MR. HOCHHEISER: You don't know. One of the big debates going on among actuaries is as follows:

There are some actuaries who say, for example, how can I consider these people and subtract from them the portion that would have retired in accordance with my probabilities (in effect, in order to make believe that mathematics equals reality, taking a portion of each one of these people)? That's the way you would calculate a loss or gain. In fact, the actuary's assumptions about early retirement usually are not so refined that you can say you really believe that's what's going to happen each year. On those grounds, many actuaries are saying, "Therefore I cannot calculate all of this, so its garbage. Don't bother me with it."

I would say that the other side of the coin is as follows. The actuary who thinks that way had better stick to his guns and had better be an actuary who refuses to give his client a breakdown of gain or loss by source.

MR. SHELDON GAMZON: I have a general question but it could be directed to Mr. Habliston. You mentioned that 44 people were targeted but the program was offered to 100 people. Now, can you design a program that actually selects the 44 people you want to get rid of, structuring it as a non-discriminatory group? Can you offer additional benefits to these 44 people and no one else, provided it's not discriminatory?

MR. HABLISTON: I don't see how you could do that. You could do that, I guess, in a non-qualified plan if you really wanted those 44 to go out. But then, if your intent is to definitely terminate them, you might run into some ADEA problems.

MR. GAMZON: You're of the opinion that it cannot be done?

MR. SOHN: If all of your targeted people are age 55 to 65, you're almost automatically asking for an ADEA problem, aren't you? If you're closing a plan where there's a wide range of employees or there's a necessary business purpose, other than just getting rid of older people, then you can do it.

MR. GAMZON: It's purely voluntary, though. We're not forcing them out, we're just offering special benefits to 44 people. It's not a discriminatory class in reference to salary or anything else.

MR. HABLISTON: I would imagine you would have employees wanting to know why those 44 were selected, and then why those benefits weren't offered to them if they were not one of the 44 selected.

MR. GAMZON: We're not dealing with the legal issue now, we're dealing with employee relations. I'm just curious as to what the legal ramifications are. Can it be legally constructed that way?

MR. HOCHHEISER: I think it might be a problem. Even though you say there's no discrimination with regard to these 44 people, some of the others to whom the offer was not made might say there was discrimination against them. So it might be an unexpected discrimination source.

MR. IRA KASTRINSKY: I have a question about the funding of these benefits. Under the minimum funding standards, you're allowed to fund the increases in these liabilities, assuming they arise from a plan amendment, over 30 years. But because the benefits themselves are given to people who are at retirement age, and the benefits are to be paid out over these peoples' life expectancies, you're in essence providing these benefits over a shorter period of time than the period you're allowed to fund them. Has there been any concern from the plan sponsors or have you been raising that point to the plan sponsors - the fact that they are really diluting the funding of the plan by allowing this?

MR. SOHN: I don't know what individual actuaries have told their clients, but this problem isn't unique to early retirement windows. It also arises any time you increase benefits for retirees.

MR. KASTRINSKY: The cost of living problem is similar. But considering the fact that these programs are becoming more widespread now, with the state the economy has been in the last few years, combined with the magnitude of the types of benefits being offered, isn't this a problem we should be more concerned about?

MR. SOHN: I think any actuary would have to be concerned with the aggregate level of funding of the plan. If it's a relatively small liability compared to the total liability, it might work out. But for a very aged group where you're funding all liabilities over 30 years you are in danger of jeopardizing the solvency of the plan if the plan isn't well funded to start with.

MR. KASTRINSKY: It seems to me that a lot of these programs are going into industries where, let's say manufacturing, you have large retired populations and the active plan population is becoming increasingly aged as we encourage people to retire. Has anybody noticed any indication from the IRS that perhaps they will be changing these funding standards? The point you're raising is that any time you do amend the plan with respect to retiring people, then you would dilute the funding. It's well known, but has anybody reacted to it in this fashion?

MR. SOHN: I haven't heard of it. In order to change the funding standards, you have to amend Section 412 of the code.

MR. KASTRINSKY: I understand that, but my question is whether anybody is becoming sufficiently concerned about the IRS as to whether there might be legislation in the future.