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FUTURE OF RETIREMENT INCOME PLANS

Moderator: R. DAVID PARSONS. Panelists: LINDA M. KAHN, RUSSELL W. THURAU, JOSEPH R. ZATTO. Recorder: JOE W. SULLIVAN, JR.

A study of the long-term future of retirement programs, recognizing:

1. Trends in plan design

2. Changing patterns in the work force

3. Impact of legislation and regulation

4. Role of Social Security

MR. RUSS THURAU: Before entering this arena of retirement income plan predictions, I am reminded that there are but two kinds of forecasters, those who don't know, and, those who don't know they don't know. I would like to be considered in the first category, I don't know. But, based on certain assumptions, which are not necessarily actuarial, unrelated to any funding method, I will attempt to describe what might happen and the resulting scenario over the next decade.

Not far from where I hail are the winter nesting grounds of the 80-odd whooping cranes that still exist on our planet. Those birds are hanging on, but there just aren't a whole lot of them left. The defined-benefit pension plan, I submit, will eventually become the whooping crane of the qualified plan industry. It has been, and is now, an endangered species. In my view, a seeming lack of private concern, aided and abetted by a negative bureaucratic undertow, will bring the defined-benefit pension plan even closer to extinction.

Why? There are a number of factors, so we'll look just at some of the most important ones. These, I believe, are the key factors in the coming demise of the defined benefit pension plan:

- The Employee Retirement Income Security Act of 1974 (ERISA) brought about an elevated level of associated expenses, and that level continues to persist in 1984 without any relief.

- The Multi-Employer Pension Plan Amendments Act (MEPPAA) and their associated unfunded vested benefit liabilities imposed on employers is the largest deterrent to growth in the negotiated plan area that there has ever been. We are now witnessing negotiations of future monies into defined contribution plans -- an unprecedented situation for negotiated plans.

- The Tax Equity and Fiscal Responsibility Act (TEFRA), with its "top-heavy" rules, could bring a rash of small plan terminations -- possibly more than were precipitated by ERISA as a result of the compounded administrative burdens and expenses.

- The Financial Accounting Standards Board (FASB), following through on its proposed accounting rules for defined benefit pension plans (whereby unfunded liabilities could become balance sheet liabilities, and funding assumptions and possibly actuarial assumptions would be combined on a single, common basis to add to the liability confusion and hike administrative expenses), could pour additional fuel on the defined benefit plan termination inferno.

- The recent increase in the popularity of defined contribution plans will continue to serve as a growth incentive for defined contribution plans (especially the 401(k) type plans) -- all to the detriment of the defined benefit plan.

- Economic conditions have led to extensive terminations of defined benefit pension plans -- both over-funded and under-funded -- by major employers, with, frequently, the future substitution of a defined contribution plan. The ability to recapture excess plan assets in times of perceived need will continue to be an economic escape hatch. If (or when) we have another cycle of double-digit fixed-income investment returns of over 15%, this particular avenue of pursuit could rapidly expand.

- Marketing of defined benefit plans via traditional routes is on a downward trend. I refer not only to consultants, but to insurance companies also. We have already seen a mass exodus of major insurance companies out of the role of providing the necessary administrative services associated with their plan products. Come the new competition of other financial centers "selling" defined contribution plans, and the defined benefit plan simply is no longer "in."

These factors, along with others, will lead to the demise of the defined benefit plan industry as we know it today. What will exist in the future, will in a large part, be concentrated in the professional corporations and self-employed area - where there are relatively few rank-and-file employees - where it is primarily a tax shelter game as opposed to income replacement.

And, if these are not enough detriments to the future of the defined benefit -- let's add one more -- a little more distant in the future than some of the other reasons cited -- that is, the passage of MUPS, a Mandatory Universal Pension System -- a defined contribution system, such as comprehensively developed in the President's Commission on Pension Policy (1981).

If you think for one moment the bureaucracy that promulgated MUPS is dead -- I submit they are still very much alive but have temporarily gone underground -- much like ground hogs -- surfacing every once in awhile to test the political air.

Evidence TEFRA's "top-heavy" and "super top-heavy" rules , which were not a product of Congress but solely an 11th-hour insert of the Washington bureaucracy -- with absolutely no hearings. Evidence further the current legislation that today pushes for earlier coverage, accelerated vesting, and extended spousal security; and/or the recent Social Security changes (equal payroll taxes for self-employed individuals, taxable benefits, the gradual boost in the retirement age) all of which were advocated in the 1981 Commission's report. Further, keeping in mind the fact that the proposed mandatory system was a defined contribution plan with 3% mandatory "employer" contributions, isn't it coincidental that 3% again shows up in TEFRA's top-heavy rules? That 1981 report -- titled "Coming of Age: Toward a National Retirement Income Policy" -- may well prove to be the retirement income manifesto for the future.

Now let's project ourselves out to 1990 and look at the qualified plan scenario:

- First we see the widespread abandonment of defined benefit plans previously alluded to.

- With the top-heavy provisions of TEFRA for small employers, we find a stagnant area of development and the continuing lack of coverage among small employers. The 1981 Commission's report indicated that 93% of all non-covered workers under qualified plans were employed by firms with fewer than 500 employees; 79% of the total non-covered were employed by firms with fewer than 100 employees. Now -- enter further deterrents to small employers via certain design requirements (like TEFRA's "top-heavy" rules), and the bleeding hearts can point frantically to the existence of a need that has not been addressed by private industry.

- Third, we now find the widespread growth and acceptance of defined contribution plans, especially among large employers. The existence of this trend will make a comparable "optional" system palatable to large segments of the private section -- perhaps, even encouraged by large employers to force the smaller competitors to have increased costs comparable to their own.

- And do any of you believe that in the next decade the politicians will have resolved all of the financial problems associated with Social Security? Continuing problems with Social Security, which is, after all, a defined benefit system, could mandate that an alternative system should be dissimilar; and a defined contribution system is indeed dissimilar.

- And one more influencing factor: do any of you believe we will no longer have federal debt problems in the next decade? With our large federal debt and the governments continued competition with the sector for savings dollars, a mandatory system providing an ongoing cash flow into federal hands has got to be attractive.

Combine all this with a period where the current political pendulum has swung back from the proverbial right of center to the left and we now have the ingredients necessary for MUPS.

Once we have defined contribution mandatory system, of which the employer could opt to have his own "comparable" defined contribution or defined benefit plan, the potential problems associated with proving an employer's defined benefit plan was comparable to any mandatory defined contribution plan will be a further deterrent to the remaining defined benefit plans in existence.

In summary, you have just been through the future phase-out of defined benefit plans as they have existed or as we know them now.

The foregoing is but one scenario, based on certain assumptions -- and absolutely devoid of complex actuarial calculations. Will they eventuate into reality? I don't know; and I know I don't know.

But the comforting part, if any, is that no one else knows either. So what I suggest you do is this: Consider all the possibilities -- even the remote ones -- in the light of current trends and movements, including legislation and political swings. Then do your long-range strategic planning based in light of what you believe will happen on what you want to accomplish.

Then somewhere in the not-too-distant-future, we can all look back and see whether our shared crystal ball was right or wrong as the case may be.

MS. LINDA KAHN: I am addressing the multiemployer plan aspect of this question. Our employers in the maritime industry on the West Coast are interested in providing retirement security for their workers. However, they are also concerned about the liabilities they may be creating for themselves and the effect such liabilities may have on their ability to do business. Hence, our employers are looking for ways to minimize the financial impact of their commitment to provide retirement income to their workers.

I would like to provide you some historical detail which, hopefully, will give you insight as to why the employers in our industry have developed this attitude over the last few years toward funding their retirement income plans. Because of (1) what has happened to the employers in the maritime industry on the West Coast, and (2) why these things have happened, many employers who are obligated to contribute to multiemployer defined benefit plans, are searching for alternatives to those defined benefit plans.

As most of you probably know, the primary thrust of the Employee Retirement Income Security Act (ERISA) is the protection of the rights and benefits of participants and beneficiaries. One of the means used to help accomplish this was its establishment of a program to insure the benefits of plan participants and beneficiaries in the event of plan termination.

As many of you know, ERISA created a new federal insurance corporation within the Department of Labor, known as the Pension Benefit Guaranty Corporation (PBGC). The PBGC was initially required to guarantee benefits for most single-employer defined benefit plans. The PBGC had discretionary authority until December 31, 1977 to cover multiemployer plans. After December 31, 1977, mandatory coverage for multiemployer defined benefit plans was scheduled to begin.

However, because of concern as to the potential risk involved in covering multiemployer defined benefit plans, Congress wanted time to review the financial impact of their mandatory coverage. Hence, to allow time for such a study, the date that such mandatory coverage was to begin was deferred until August 1, 1980.

Initially, under ERISA, a company which withdrew from a multiemployer plan had no obligation to continue funding its fair share of the plan's unfunded liabilities, unless the plan terminated within five years of its withdrawal. The continuation of this law would have encouraged early withdrawal of those employers who wished to limit the period of their liability. In fact there were a number of employers who did just that.

After considerable study of the financial condition of the existing multiemployer plans, the likelihood of a plan's termination and the magnitude of the unfunded liabilities if it should terminate, Congress passed the Multi-Employer Pension Plan Amendments Act (MEPPAA) which did several things:

- It scaled back the amount of benefit which the PBGC will pay when an unfunded multiemployer plan terminates;
- It increased the insurance premium which a multiemployer plan must pay to the PBGC from $0.50 to $1.40 per participant per year; and
- It enacted hefty withdrawal liabilities.

These withdrawal liabilities are, in part, calculated according to a company's highest contribution rate in the ten years preceding withdrawal. Most importantly, they generally are unlimited as to amounts. That is, if an employer withdraws from a multiemployer plan, this penalty must be paid, regardless of whether the plan terminates.

Such onerous requirements may affect a company's ability to borrow money, to buy another company, to be sold to another company, or to merge with another company. A contributing employer's flexibility is thus limited and its financial health may be impaired.

To put it bluntly, from a contributing employer's perspective, MEPPAA shifted the responsibility for unfunded liabilities of multiemployer plans from the shoulders of the federal insurance corporation which was established for the purpose--the Pension Benefit Guaranty Corporation (PBGC)-- to the "parties", that is, both to companies that sponsor the plans and to their workers.

Congress provided that special withdrawal liability rules may be permitted, however, in an industry that has characteristics that would make use of the special withdrawal rules appropriate, if the use of the special rules will not pose a significant risk to the PBGC. That is, to obtain approval of the use of special withdrawal liability rules, an applicant must satisfy the PBGC of two things:

(1) The industry has characteristics that make such rules appropriate; and

(2) Such rules will not pose a significant risk to the corporation.

ERISA, as amended by MEPPAA, generally imposes liability for a portion of the value of a plan's unfunded vested benefits on an employer that ceases to have (1) a contribution obligation or (2) covered operations. Under current law, a business failure would normally result in withdrawal liability.

Our Association has many small closely held companies as members, whose operations are adversely affected by MEPPAA's withdrawal liability provisions. Hence, in April 1982, the International Longshoremen's and Warehousemen's Union-Pacific Maritime Association Pension Plan filed with the PBGC an application for approval of special withdrawal liability rules. The application was approved January 30, 1984, after nearly two years.

The special rules that we sought impose withdrawal liability for a business cessation only where the employer

(1) continues or resumes covered operation, without an obligation to make contributions, or

(2) sells all or a portion of his business or assets to a competing non-contributing employer.

Under the special rules, an employer that simply goes out of business will have no withdrawal liability.

To assure the PBGC that the use of the special rules would not pose a risk to the financial health of the plan or increase the likelihood of the plan's termination, the plan was amended to provide that the contributions for each plan year shall be not less than the total administrative costs and benefits paid during the year. It also was amended to incorporate an accelerated funding requirement.

In order for the special withdrawal liability rules to remain in effect, employer contributions to the plan for each of the next 20 years must be sufficient to assure the plan funding remains "on target." The first target is at the end of the 10 years, or 1994. The value of plan assets must be at least 50% of the value of accrued vested benefits by the end of 10 years. By the end of the 20 year period, the value of plan assets must be at least 80% of the value of accrued vested benefits. All present values are to be determined on the basis of the actuarial assumptions used for the plan's valuation on the date of the application. To demonstrate compliance with this requirement, the plan actuary will submit each year a cash flow projection to the PBGC.

As you can appreciate, it involved a lot of work to obtain approval for use of the special rules. Now that approval has been obtained, there will continue to be a lot of additional work to assure that the plan can continue using the special rules. The effort involved in obtaining and, hopefully, continuing the use of the special rules is evidence of the depth of concern by our employers and their workers as to the effect on the health of our industry of the withdrawal liability imposed on employers contributing to multiemployer defined benefit pension plans under MEPPAA.

Employers are concerned about their withdrawal liability. Many multiemployer plans may not have parties to their agreements with the unity of spirit necessary to obtain approval of the use of special withdrawal liability rules. Many multiemployer plans may not be able to satisfy the two conditions necessary for the approval of special withdrawal liability rules.

In the collective bargaining arena, employers and their workers are receptive to limiting future commitments to defined benefit plans. There is considerable interest in the use of a supplemental welfare plan to pay cost-of-living increase in benefits to retirees.

There is a lot of media coverage about IRA's and 401(k) plans. However, under current law, a 401(k) plan may not be feasible for a multiemployer plan. A 401(k) plan is basically a salary or "wage" reduction plan. But the plan is predicated on there being profits or a "stock bonus" from which contributions are to be made. Why could there not be a "wage reduction" money-purchase 401(k) type plan? I, for one, would like to see such a plan permitted. The interest is there--on both the management and the labor side.

MR. JOE ZATTO: I think I must have been put on the program to give a counter balance. I don't envision the sky as being filled with whooping cranes, but I do think the future is quite a bit more positive than might be anticipated right now. Consider the history of our country; today the buffalo herds are growing and the trains are becoming extinct. Before trying to predict the future of retirement income programs in this country, we can begin by appraising where we are today. Basically we have just emerged from a very turbulent 15 year period that has included a lot of problems, and you have to have a pretty healthy program to have come through it. For example, we have had extreme volatility in inflation, interest rates and investment returns. We had extreme volatility in the funding of defined benefit plans, both from a perspective of costs and from a perspective of assets versus accrued liabilities.

We have had the introduction of an era of intense regulations; it seems like it would go on forever. Since 1972 perhaps, we have had a growing concern and uncertainty about the future role of Social Security. We have had changes in tax laws that have made profit sharing and defined contribution plans much more attractive. We have had increased involvement of accountants in defined benefit retirement programs. We have a situation where accrued pension liabilities have become, at least partly, a legal liability.

Periodically, we had a high concern about unfunded liabilities and, ironically, at present we detect a growing concern about over- funded pension plans. I think that something that has happened during the last 15 years that influenced this defined contribution/defined benefit question is the introduction of some very attractive funding vehicles for defined contribution plans. Finally, I would add that we have had some large economic dislocations which have required some special shifts in retirement programs, early retirement benefits, and "window" programs. So the past several years have been turbulent and retirement programs have changed because of it.

Although there continues to be an increase in the number of qualified retirement programs and an increase in the number of participants covered by retirement programs, there has been a pronounced decrease in the number of new defined benefit plans. Ten years ago, just looking up some statistics, 55% of the plans being installed that year were defined benefit plans (15 years ago, it was probably more than that). Last year 25% of the new plans being installed were defined benefit plans. There is no question that defined contribution plans are growing and they are growing rapidly. However, this doesn't mean that defined benefit plans are disappearing or that they are being eliminated. In most cases, I think what is happening is defined contribution plans are being installed or extended as a complement to a defined benefit plan. We are at a point today where defined benefit plans are being de-emphasized while defined contribution plans are being expanded. This is only logical when you consider the forces that have been at work in the short term. But that is where we are today. What does it likely mean for the future? This gets into prediction-knowing you don't know or not knowing that you don't know. But it is easy to predict the future because it will take a couple of years to prove the prediction wrong.

Basically, I am convinced that defined benefit plans are going to continue to be the mainstay of retirement income programs; but they will operate in a different setting. First of all, I think there is going to be a tremendous increase in consulting skills and consulting assignments in our fields. There is going to be an increase in objective setting for companies. This objective setting will address retirement income levels, pre-retirement needs (because defined contribution plans have some very positive aspects for them in connection with pre-retirement needs), portability, the tax deferral of employee contributions (which, together with the investment vehicle has been a big incentive in defined contribution plans) and development of combination programs.

My view is that what we are going to see in the future is defined benefit plans continuing, being modified, being adjusted, etc., but in no way being a stand-alone program. They will be the core program, supplemented by a defined contribution plan together with tax deferred employee contributions. The logic and the balance is there. Defined contribution plans also allow companies to address a problem of post-retirement inflation protection that will come up again in the future, that has existed in the past, but is relatively dormant now. A couple of years ago there were some really creative and imaginative solutions being taken by some companies combining account balances and defined contribution plans, transferring them over to defined benefit plans and using them to help share the cost of post-retirement inflation protection. There is a bright future for the combination of that type plan. What we are seeing today is a great expansion in thrift plans with 401(k) features. It makes sense because of the tax incentive.

Another thing that may come up in the future is a feeder plan or a floor plan which in effect is the combination of both a profit-sharing plan and a pension plan or a pension plan promise. What it says in effect is that the sponsor will promise a certain level of retirement income at retirement. If the profit-sharing accumulation doesn't meet this level then the pension plan will provide a supplement so the combination will attain that level. Some people say it will give the employees the best of both worlds. I don't think that is the case, I think what it really does is that it allows an employer to establish an adequate level that it can guarantee its people and in effect only provides as much of that as is necessary (i.e., that isn't provided by the profit sharing plan). Another type of program that might become more popular in the future and which moves away from a defined benefit plan is a target plan. A target plan is really a pension plan rather than a typical profit-sharing plan. It is a defined contribution plan, which works somewhat like a defined benefit plan. The plan establishes a target benefit at retirement. The contribution rate is determined as the amount necessary (at different age and pay levels) to accumulate funds to meet the target retirement benefit. Contributions are made on that basis to individual accounts, so it does avoid the liability problems that are inherent in defined benefit plans. Target plans may become popular, but what my own feeling is its going to be basically thrift plans and an extension of floor or feeder plans.

Whatever happens, there are an abundance of consulting opportunities out there in the future. There will be requirements for actuarial calculations that will become more complex than they have in the past because many times instead of a stand alone retirement program, calculations will be done for a combination of two programs. My perspective of the future is a good one. There are going to be changes and there will be confusion, but there are always changes and confusion that come along with growth. By no means do I see the defined benefit plans dying out, I just see them changing.

MR. ROBERT SCHNITZER: The experience that we have had in Los Angeles with smaller and medium size corporate clients has been in fact on the pessimistic side, they don't want to have anything to do with actuaries. They feel that actuaries can't communicate- I don't know where they got that impression (laughter)-- and that defined benefit plans are particularly complex to administer and to communicate. However, we have seen larger companies that are frankly skeptical of all the fuss that is going on. What I would like to say is that I think that our own attitudes toward the question can have a lot to do with the future if we go to our clients and prospects with the attitude that defined benefit plans have no future. I think that will be a self-fulfilling prophecy. On the other hand, if we try to be creative and innovative and help these clients modify their program if need be, then we may be able to keep our own jobs a little while longer.

MR. DON GRUBBS: A couple of items -- one on the MUPS matter. You indicated that the President's Commission on MUPS proposal was a defined contribution proposal and indeed that is what they recommend. However, that is not the only kind of MUPS proposal. Those of you who still have your 1970 copies of The Actuary filed away or if not at least the 1972 copies of the Transactions will find there a detailed MUPS proposal advocating that employers be able to meet their responsibility with minimum benefits or with minimum contributions. The reason that the President's Commission came down in the direction they did relates to something which is honestly a weakness of defined benefit plans. I am an advocate of defined benefit plans, but at the same time, I am aware of one of their short-comings. Ideally someone who spends his career with several different employers and has vesting under various plans ought to get as much pension as someone who spends about 40 years with one employer. He is going to end up with the same needs. He had the same overall kind of working history though

split up among several employers. But the problem in an inflationary age is that the benefit accrued with the earlier employers will not be significant for the employee and because the accrued benefits which are cashed out produce very low values at the younger ages, any amount which is cashed out at the young ages may not be sufficient to provide very much of the needed pension. In response to that , I suggested a modified defined benefit approach which sets for defined benefit plans a minimum benefit equal to what would have been provided by the 3% defined contribution with the stated rate of interest.

This is a way in which defined benefit plans can overcome the problem which they actually have with respect to inadequate benefits provided for those who terminate at young ages. We are going to preserve defined benefit plans not just by saying that they are good but by solving whatever short-comings they have.

MR. DAVID PARSONS: You would advocate that approach over indexation of accrued benefits, I assume. That is something that appears to have been at least proposed in Canada.

MR. GRUBBS: The indexation of accrued benefits has, indeed, problems of financing. Howard Hennington addressed the problem, I think, quite well at the International Congress of Actuaries in 1980 and wrote a very fine paper on that subject.

MR. STEWART LYON: I wonder if I could spend a few minutes putting a transatlantic perspective on what we have been discussing this morning. I find it very interesting that history seems to be repeating itself. When I first came into the actuarial world defined contribution plans were on the way out, because they were not producing the kind of incomes that retired people really needed. Defined contribution plans, particularly where the funds were being invested in fixed interest securities were producing inadequate benefits and those benefits had to be repeatedly topped out. Over the period of my lifetime, we have moved to the position in the United Kingdom where well over 90% of employees who are covered by retirement benefit plans are covered by plans of the final pay type and most of those are providing benefits that accrue at the rate of 1-2/3% of salary per year of service.

We also have a system whereby most of those employees are contracted out of the earnings related part of the Social Security. Something like 10 million employees out of the 12 million or so members of occupational plans are contracted out of the state scheme. The state's earnings related scheme is a sort of revalued average earnings scheme. Now, of course, final pay schemes have their own problems as had been mentioned a moment ago in relation to Canada. Not least is the problem of those people that change their jobs many times in their careers. This has been a very live political issue in Britain in the last few years. There is in Britain a statutory body called the Occupational Pension Board which took a look at this problem a few years ago and recommended that something ought to be done about early leavers in the sense of revaluing the preserved benefits after they left the service from the time between then and retirement age by the cost of living index or 5% per annum, whichever was the less. The government said that it was going to legislate on those lines quite soon. This will help, but it won't go away. The government is also anxious to introduce legislation (nothing like or as comprehensive as ERISA, I think) to enable or to force schemes to disclose much more information to members about what is going on.

Most recently, last December, the government set up a committee of enquiry into provisions for retirement to have a look at a number of major aspects of retirement provisions -- one of which is the increasing burden of costs of Social Security and also the impact on the next generation of the maturing of funded retirement benefit plans, because one just can't assume that if you fund a pension, it's not going to present any problems to the next generation. Also we are having a look at the question of equalizing retirement ages related to unisex that was being discussed earlier on. But the most live issue amongst all these is the question of portable pensions. There are political over-tones here. You won't find it too difficult to realize that amongst our present government in the U.K., a number of people who believe in people standing on their own two feet, not relying on either Social Security or even on employers too much. This has surfaced in the form of a proposal that employees should be entitled, if they leave an employer, to take a cash lump sum equivalent in value to their preserved benefit and do what they like with it, within limits. In other words not necessarily to leave it behind and not necessarily to take it to another employer but to put it into an individual retirement plan or something like that. I think this is quite likely to come about.

The other strand though is that employees should not be forced to join final pay plans: they should be given the right to opt and to put their money and perhaps a contribution from the employer into any kind of pension plan that might be devised, which obviously would be a defined contribution type arrangement.

One of the arguments advanced for this is that there is far too much of the nation's savings being channeled through institutions and not nearly enough in the form of individuals owning their own portfolios of shares and thereby being able to encourage the setting up of small businesses, etc. I believe that the thinking behind that kind of proposal is not wholly logical. It's very easy for those of us who are financially sophisticated to say that we would like to be able to do certain things with our own money and to extrapolate from there and assume that the man on the shop floor or sitting at the office desk would like to do the same thing and moreover would be able to do it.

Many of us think if we get the whole pension system loosened up in the way that some politicians would like all that would happen would be the younger employees who don't realize how much it costs to provide for retirement would not put enough aside for one thing, and those who did would probably put the money into our equivalent to your Savings and Loan institution rather than putting the money into serving British industry. The debate has just started; the battle, as it were, has just been joined or rejoined between defined benefit and defined contribution plans. I myself am a firm believer in defined benefit plans for reasons that have been given by other speakers. Whether defined benefit plans will become obsolete I don't know--I doubt it. I see the main future as lying with defined benefit plans but with considerable overlay of defined contributions.

MR. PARSONS: There might be a clarification needed for this audience. My understanding is that in the U.K. mandatory employee contributions are the rule, so employees are required to join plans and contribute 6% or 7% of pay. But if I understand what you are saying, if companies are not allowed to mandate 5% or 6% of pay contribution to plans, then the implications for retirement plans in the U.K. are fairly severe because plans are likely to lose their base of young contributors and be left with only those at older ages for whom it is obvious that they ought to stay in the plan.

MR. LYON: That is probably correct.

MR. PARSONS: A lot of the pressure that is on defined benefit plans relates to those plans that base benefits on final average pay. Do you foresee a reversal of the trend of the past fifteen or twenty years with the conversion of final pay to career pay plans?

MR. ZATTO: While I haven't had the experience yet of converting final average plans back to career average plans, I think that I will have in the not too distant future. To answer your question, if I had a clean slate considering there are pressures, because the economic condition certainly has changed and become much more uncertain, I would probably be trying to formulate programs that were basically career average--final average minimums where the minimum was at a core level. Following through on what I said, I would be trying at the same time to establish a defined contribution plan in conjunction with it because I think that can address for the younger employees things that are important, the account balance, the visibility of the account balance, the ability to get funds during employment. I would try to come at it from the direction of career average with a final average minimum and a defined contribution plan in conjunction.

MR. THURAU: A career average defined benefit plan is only a modification of a defined benefit contribution plan so why not make it simple and attractive and go with a 401(k) defined contribution plan. Why clutter it with a career average defined benefit plan and then go ahead and cap it off with your final average? Nowhere have I seen where two career average plans equals one final average plan.

MR. PARSONS: One of the things I haven't heard anybody on the panel address is the issue of Social Security and where that is taking us. Again going back to what a lot of us have been doing, we have been recommending final pay, offset plans. In the context of some significant reduction in Social Security replacement ratios lately and with a lot more concern amongst plan sponsors that Social Security may go away or provide small benefits, do any of the panel members see us going away from or recommending to clients going away from offset plans to step-rate plans to try to avoid the situation where reductions in Social Security automatically result in higher liabilities and contributions.

At the same time, one of the things that Joe Zatto alluded to was the increase in the Social Security retirement age. It would seem to me advantageous, though I haven't seen any clients do it, to begin now to link retirement ages to Social Security so that again you are not stuck with retirement age of 65 when everybody is retiring at 67 or 68 under Social Security.

MR. THURAU: I do not see the same strong movement to offset plans that final average plans have experienced in the last decade. I see a definite slowdown there and I see more of a confused or just less organized movement or common bandwagon right now. One approach is going to combination plans with a non-integrated pension plan at levels to cover rank and file people and some kind of integrated defined contribution scheme in conjunction with it. But the only thing clear to me is it's not the same bandwagon that ran rampant about 10 years ago.

MR. ZATTO: I have trouble seeing companies doing away with integration. To the extent that career average plans come back, which I think they will to a degree, I don't think you are going to have the offset approach. So there will be one change in integration approaches with a career average plan. I can see final average plans being designed in a way that continues to use offset and for that matter use it in several ways. I know of plans that use 100% offset that have to be updated every three or

four years. I can see those continuing. There is a nice logic to that if you establish a reasonably adequate modest replacement schedule, so I may be contradicting myself, but I can see both things happening.

MR. PARSONS: Of course we may have any Social Security integration legislated away for us one of these days. That was one of the things which was in the draft of 1053G in ERISA that finally got knocked out that would have limited or frozen Social Security offsets.

Linda, one of the things I am interested in is do you see in your industry the continuation of every three years significant increase in benefits being negotiated or is that something the employees are going to have to swallow and take a freeze on for a number of years until the plan presumably becomes more financially sound?

MS. KAHN: I can't speak for the East Coast, but on the West Coast, no I do not see that continuing.

MR. PARSONS: Do you think that will be replaced with the demands in other areas or other benefits or that this is just a general reduction in benefit levels.

MS. KAHN: Well I think we will find some other way to provide a benefit. I don't think it will continue to be provided through a different benefit plan that will be subject to the MEPPAA withdrawal liability because our employees are just too concerned. We have too many small employers which are closely held and even with the special rules they are still very concerned about the accounting implications of having to reorganize these liabilities.