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NATIONAL RETIREMENT INCOME POLICY

Moderator: DONALD S. GRUBBS, JR.
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Recorder: DONALD S. GRUBBS, JR.

- o Why have a national retirement income policy?
- o What is the present national retirement income policy?
- o Who should determine national retirement income policy?
- o When should workers retire?
- o How much retirement income should be provided?
- o What are the appropriate roles of social insurance, employer plans, individual savings and other sources of income?
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- o Should retirement benefits be provided as annuities or as lump sums?
- o Should portability be provided? If so, how?
- o What retirement income should be provided to unpaid homemakers?
- o Should policy favor defined benefit or defined contribution plans?
- o How should pension plans and benefits be taxed?

MR. DONALD S. GRUBBS, JR.: I'm Don Grubbs. I have a little consulting practice in Silver Spring, Maryland. Ken Steiner is with The Wyatt Company in Boston. In addition to being a consulting actuary, Ken is Chairperson of the Academy's Task Force on National Retirement Income Policy. Anna Rappaport came down with a bad case of flu and, unfortunately, cannot be here.

During the last two years there has been a rising interest in the question, "Should we have a national retirement income policy?" Various groups have been discussing it. Some have come up with what they think is a national retirement income policy of their own.

To start with I'm going to ask the question, "What do we mean by a national retirement income policy?" and "Why should we have one, or should we?" By "national retirement income policy" I think we mean something that sets forth the main goals, the main purposes which will be our policy guide. It is not something that sets forth the detail as to how you should define HCE, but something that points the way to where we're trying to go, so that as the details are developed they might help us get toward that goal. Those of you who have done a bit of sailing may set an objective and, having set that objective, you may tack, that is, take a zigzag course to get towards your objective. But because you have an objective this apparent zigzag course is apt to lead you to the goal. But if you don't have a goal you're more like a piece of driftwood washed around by the waves and the wind and unlikely to arrive at a favorable port. Some of us feel that's what's been happening in the sixteen years since ERISA, that we haven't been moving toward any well-defined goals. Ken, what do you think? What do we mean by national retirement income policy? Do you think we ought to have one?

MR. KENNETH A. STEINER: Well, I think that we should have one. I view the national retirement income policy very much as you do, that is, as an objective. Just as corporations have objectives for their benefit plans, or their profits, or whatever programs that they have, I view a national retirement income policy as an objective on a national level, a national government objective with respect to the level of and the sources of income to be enjoyed by current and future older members of our society who are no longer in full-time employment. So I view this as a frame, as you said, as a goal. I think that our policymakers should be constantly thinking about, if we have a policy -- I believe we do have a policy -- what are we trying to achieve with that policy? I think that, whatever policy we have, it is subject to change. Obviously, it has changed or at least it has been modified in recent years. I think it's unrealistic to assume that there's going to be something written in stone such that Congress, before it enacts any piece of legislation, is going to ask, "Is this consistent with the policy?" That would be nice, but I think what Congress is really doing when it enacts legislation is refining or developing the policy. Why should we have a policy? I think it's reasonable for such action at a national level, just as it's reasonable for other actions at a national level, public defense, etc. I think it's reasonable to be concerned about the nation's retirement income.

As a little bit of a deviation from the question, I'd like to follow-up on what Don had indicated. A while back I semi-volunteered to be the Chairperson of an Academy Task Force on national retirement income policy. The charge of the task force is to determine whether it's desirable or feasible for the Academy, as representative of the actuarial profession, to develop a national retirement income policy, much in the same way that ASPA has gone about developing a national retirement income policy. One of the reasons that I'm here is, not only to give you my ideas, which, by the way, don't represent the ideas of my employer, of the Academy, nor of the Academy Task Force, but also primarily to get input from members of the profession on some of these issues and whether it is feasible or desirable for members of the actuarial profession to develop a national retirement income policy. And if it is not feasible or desirable, how should we be involved?

MR. GRUBBS: Ken, I think I heard you say that we already have a national retirement income policy. Did I understand that right? Do you think we have one, and if so, what is it?

MR. STEINER: Well, I believe we do have a national retirement income policy, and in this respect, I guess I'm one of the few people who can glean a national retirement income policy from the rules and regulations that we currently have. I believe that the national retirement income policy is, first, a floor of protection and the great concern is that people who put in full time or pretty much full time careers in this country are entitled to receive a minimum or a safety net standard of living after retirement. And then the second policy objective that our nation has is that our government encourages savings or the providing of retirement income to employees through privately sponsored plans and through individual savings. I view it as the three-legged stool with strong emphasis on the mandatory floor of protection and equally strong emphasis on the voluntary flexible savings as a supplement to that floor of protection, the encouragement that Congress provides in the national retirement income policy to provide additional benefits. I think part of the precepts are that, if supplementary coverage is provided, it

should be on a broad basis. If employers or other privately sponsored plans make benefit promises, then I think that Congress is very concerned about the guarantee of those benefit promises, and that if employers sponsor plans, then such plans should not discriminate in favor of highly paid individuals.

I believe that the current national retirement income policy is embodied in the Internal Revenue Code and the Social Security Act. And, as I said, it's a three-legged stool. While many people think that there is not a national retirement income policy, I think it's important to recognize that the current rules with respect to privately sponsored plans are such that employers are not forced to provide retirement programs. Those who would propose national retirement income policies might alter what I consider to be a basic precept, which is, these are flexible voluntary type programs that generally employers set forth. If plans are sponsored, in general they don't have to provide minimum levels of benefits. There are certain exceptions, most notably, the Top Heavy Rules in defined benefit plans. If the plans are provided, they don't have to be of any particular type. These are all issues that, if one were to develop a national retirement income policy, one would probably have to grapple with "Should there be such flexibility?" Under the current national retirement income policy, there is significant flexibility provided to employers. Oftentimes there's flexibility in to how these programs are funded. I believe that the current national retirement policy provides employers with significant flexibility, which is good in my opinion, so that employers can structure their total compensation programs to best meet the needs of their employees. So employers are not forced to provide certain levels of retirement benefits. They can provide higher levels of cash instead. So I think the key word that I see in the current national retirement income policy is flexibility for anything on top of this mandatory safety net.

MR. GRUBBS: I'd like to read a couple brief extracts from Section 2 of ERISA:

> It is hereby declared to be the policy of this Act to protect . . . the interests of participants in employee benefit plans and their beneficiaries, by requiring the disclosure and reporting to participants and beneficiaries of financial and other information with respect thereto, by establishing standards of conduct, responsibility and obligation for fiduciaries . . ., by providing appropriate remedies, sanctions and ready access to the Federal courts, . . . by improving the equitable character and the soundness of such plans by requiring them to vest the accrued benefits of employees with significant periods of service, to meet minimum standards of funding, and by requiring plan termination insurance.

That sounds like a policy statement to me.

Title 4, the title that established the plan termination insurance, contains its own policy statement. It states:

> The purposes of this title . . . are . . . to encourage the continuation and maintenance of voluntary private pension plans for the benefit of their participants . . . to provide for the timely and uninterrupted payment of pension benefits to participants and beneficiaries under plans to which this

> title applies, and . . . to maintain premiums . . . at the lowest level consistent with carrying out its obligations under this title.

In 1979, President Carter appointed a commission to study national retirement income policy. It was called the President's Commission on Pension Policy. It consisted of 11 prominent individuals, some with extensive background in pensions, and some with little background in pensions but known as leaders in their own fields. The Commission had a staff of more than 20 people, including Pres Bassett, an eminent actuary who had been with TPF&C many years. It commissioned a lot of research. It held hearings at which all those interested with retirement income were welcome to testify, and a number of actuaries testified at those hearings. In 1981, the Commission published a report that extensively addressed what it thought was an appropriate national retirement income policy. Whether one agrees or disagrees with the particular conclusions reached, the process the Commission used was a kind of process that would be appropriate for the task. But, like Ken, I feel that you can tell what people's policies are by what they do. We can look at what Congress has been doing and see a wide range of policies which are not always the policies that we see in ERISA. We have seen pieces of the President's Commission recommendations picked up by Congress, but the principal policies were never adopted.

Ken, who do you think should determine this policy and what role should actuaries have in the process? You got into that a little. Do you have anything else to say on that at this point?

MR. STEINER: I think it's up to the policymakers to make policy, so I would view that as being Congress and the President. Obviously, these are elected individuals and we have some input, not very much as individuals and maybe a little bit more as a profession. I think my personal view of the role of the actuaries is to do what we do well most of the time, and that's to substitute facts for appearances and demonstrations for impressions. So I view our role as not of a policymaking role, but rather an educational role. I think that we can certainly be more aggressive in that role in a number of areas.

I think that the Academy essentially and the members of the profession can and probably should act as consultants to members of Congress and take on such issues as quantification of the short-term and long-term revenue gains from providing tax incentives. I think that Congress obviously is very much concerned with the short-term revenue losses of providing incentives to sponsor private plans, and I think that the profession can do a lot in terms of quantifying the long-term effects of those revenue gains, because benefits are paid and they ultimately add to the tax base.

I think the profession can assist in quantification of Section 415 limits and plan funding. Clearly, I think we could be of some benefit in recommending changes to the current rules and regulations that would simplify administration but would be revenue neutral. Also, just because we deal with so many retirement plans, we could provide facts concerning the coverage and benefits provided to individuals and who is really receiving benefits under these tax favored plans. Are they all highly paid like Congress thinks? We could make comparisons of benefits provided by privately held plans versus benefits provided to government employees like under the FERS program. We could provide

facts, if we can develop them, concerning the savings rate or the proportion of the nation's savings rate that's represented by privately sponsored plans. I think that these are steps, positive steps, that the profession can take short of actually sitting down and developing the policy, which I view as the role of the policymaker.

MR. GRUBBS: I certainly agree completely that the actuary should take a very active role in providing input into the process. We cannot determine national retirement income policy, but we can have input. A number of the people here in this room, indeed, have had a very active role. I think, though, that for the Academy or anyone else to purport to represent the views of actuaries is a false representation, because we all disagree. We don't agree on anything, and if anyone says, "This is the viewpoint of actuaries," it's merely a misrepresentation.

The questions of should we have a national retirement income policy, who should develop it, and how should we develop it, are open for discussion. Who would like to comment?

MR. DANIEL M. ARNOLD: I agree with you that there should be a policy. I agree that there is a policy, if not specific, de facto through the Code and the Social Security Act. I also agree that the actions of the Congress and how they're being carried out reflect what the real policy is. I have a perception that the fact that the current Congress and the Ways and Means Committee and the Finance Committee play dominant roles to a certain extent is reflective of the personalities on the various committees and that those personalities change with time. So to a large extent it depends on who the people are in the Congress, who gets elected.

That gets me back to where I have a disagreement with the two of you, and that is, who should set this policy? I believe the policy should be set by the American people through the people they elect. The people who are elected, however, are very much influenced by the public. In Connecticut, where I happen to live, Nancy Johnson and Barbara Kennelly, who are on the House Ways and Means Committee, and their staffers seem to be responsive to specific pieces of information about companies or about individuals. That collection of information appears to have impact. So there is a responsibility of the actuarial professional and of each individual actuary to communicate with the Congressman or Congresswoman, rather than to complain to the IRS or complain to the Labor Department, and have effective communications which will then, hopefully, influence how those people will set the policy or the laws which become the policy.

MR. DANIEL F. MCGINN: One of the things that strikes me about national retirement income policy is the fact that Congress keeps passing laws and writing policy statements, but, from my view, Congress has no real understanding of the needs of the people: it really needs to be educated. It seems to me that Congress should be educated by this actuarial organization concerning the available ways to formulate a national retirement income policy. You mentioned the so-called "three-legged stool." Reference to a three-legged stool implies that you have the Social Security system, private pensions and private savings to provide a retirement income. However, the vast bulk of people are paying so much in taxes that there is a very little opportunity for these people to save.

For most employees, a substantial portion of their earnings is being pumped into the Social Security system. Thus, for most people, private savings do not represent a source of future retirement income. In light of the current high level of Social Security taxes, the burden, from my perspective, should be borne by employers. However, it seems clear to me that small employers need a strong incentive to establish plans. Instead of a tax deduction for contributions made, some kind of a tax credit should be granted to small employers that set up plans that cover primarily the average employee -- not the highly compensated. Existence of such credits would encourage them to establish these plans. And I think it is quite obvious that defined contribution plans are the types that are growing in number while defined benefit plans are being terminated. Because of this fact, any national retirement income policy should prevent people covered by such plans from cashing-out their accounts when they sever employment. If terminating employees receive lump sums, most will reach retirement with no lifetime income at all. So it seems to me that these are fundamental concepts that need to be incorporated into the development of any national retirement income policy.

To my knowledge, the greatest shortcoming of defined contribution plans has not been addressed: in general, they are cash severance plans, not retirement plans. I don't see how the Congress can possibly address these matters unless it has an education, and, until now, it certainly has not been educated. In my opinion, the people in Congress don't know what they've been doing -- except from an expedience point of view. In recent times almost everything that Congress has done, in spite of words to the contrary, has been to attack the small corporate plan sponsors and to raise taxes. Congress has ignored the long term implications of what it's doing.

MR. IAN M. CHARLTON: No doubt there is a need for a level playing field in retirement policy, and I believe as one other speaker has mentioned, the electorate, the ones who are going to pay for it in the long run, should be the ones who define that policy. They place people in Congress for the purpose of carrying out their wishes; therefore, in my opinion, the Congress is probably the right place for initiating a retirement policy. With respect to guidelines, I think that the Congress has already adequate guidelines in the plan to which it is subject. Therefore, it would seem to me that a starting point in defining guidelines for a retirement policy is the benefits and the rewards of the plan which the Congressmen enjoy. Really, I think the three-legged stool that has been spoken about is missing one leg. We did have it I think in the earlier days of the 1980s, in the lesser restricted use of 401(k) plans and IRAs. And I believe that the American public should be allowed to save on a tax deferred basis for retirement purposes. I don't see, as the gentleman just prior to me spoke, that lump-sum distributions are part of retirement policy. If you're putting money aside for the future years, you should have some kind of a tax relief currently; that is exactly how it should be. And I do feel as though while Congress may have established some kind of retirement policy and some kind of a way of providing for deferred taxation of contributions, we also should require our government employees whose income is derived from tax monies to attempt more closely to define the details of the retirement policy in a less volatile and vacillatory manner than we have seen over the last few years.

MR. RICHARD DASKAIS: I think it's important to identify some other important players in the formulation of policy, if we can call it that. I think the permanent staff of

some of the Congressional committees, such as the Joint Committee on Taxation, has a great deal of influence, and obviously, (this speaks to the point that Dan McGinn raised about smaller employers) large employers and large unions have been fairly effective in at least getting their views heard. Last, of course, you have some special interests, such as, let's say the pet project of influential Senators or Congressmen. For example, Senator Long was responsible for employee stock ownership plans (ESOPs) which seem to have, in my view, very little place in a retirement policy.

MR. STEINER: I thought all those comments were excellent. They're the kind that we're looking for, and we certainly encourage everyone to stand up and put your thoughts on the record. I guess I'd like to, if you will, defend the position of Congress for just a second and throw in what is, obviously, the other side of national retirement income policy and that's a national tax policy. National retirement income policy, at least with respect to private plans, costs money or at least Congress believes it costs money. There is now and there always has been a tension between national tax policy and national retirement policy. While I think it's all very easy for pension actuaries to get upset and concerned that Congress is whittling away at the incentives for retirement programs, I think it's also important to recognize that there are many actuaries in our profession who would prefer not to pay higher taxes or not to have their companies pay higher taxes, rather than some of these things that pension actuaries have grown so dearly fond of, some of the incentives. So I believe that Congress has acted responsibly in this manner in terms of balancing the needs, balancing the tensions between tax policy and retirement policy. The deficit has grown significantly larger over the last ten years from what it was prior to that time. Congress has been forced to choose between raising taxes and finding revenues from other sources, so I don't think that you can really say, at this point, let's design a national retirement income policy without keeping in mind that Congress also has to develop a national tax policy which involves having sufficient revenue, having some fairness, equity, etc., all the stuff that it said that it was trying to do with the Tax Reform Act.

MR. GRUBBS: I certainly concur that you can't look at retirement income policy in a vacuum. There has to be a balance with tax policy and with other policies like employment policy. Nevertheless, I would differ with the statement that Congress has acted responsibly. I don't think it has.

MR. MCGINN: I am very sensitive to statements that imply the Congress has acted responsibly on behalf of the private retirement plan system. Back before the Multiemployer Pension Plan Amendments Act of 1980 (MPPAA) was enacted, I and probably a half dozen other actuaries met with the staff advisors to the Congress to discuss the impracticability of that legislation. The chief actuary for the IRS was present at the meeting. We spent an entire day reviewing the reasons why MPPAA was totally unfeasible and impractical. We explained why that legislation would ultimately destroy many multiemployer pension plans and create all kinds of confusion in the multiemployer pension plan field. I believe that every Congressional advisor present at the meeting agreed with our position, but, in the end, they stated that such facts did not really matter. Congress had already decided to pass this legislation because it was good politics. Congressional actions would not be governed by reality. That's exactly what happened: MPPAA was enacted, and I am sure that, behind closed doors, many times

similar decisions are reached in spite of expert advice to the contrary. If politicians recognize that an important constituency exists, it will enact legislation to get votes, especially when the long-term implications are masked by the complexity of the subject matter. They just will do it. Well, to the extent that they're representing their constituency and the desire of their constituency, then they have a rationale to do so.

MR. GRUBBS: Let's move on to one of the substantive questions of what a policy might be. When should workers retire and when should benefits be made available?

MR. STEINER: I think workers should be able to retire whenever they want to and whenever they can afford to. I think that I would separate, as I do with many of these questions that we're going to talk about, the floor piece versus the flexible piece. And with respect to the floor piece, the safety net, I think the real question is what benefits should be provided as opposed to when should workers retire. So I guess I will pass on the question of when should workers retire. But I view how much should be provided as largely on the floor piece, largely cost driven, as to what can we afford and what can we do to keep things equitable between retirees and people who are currently working. That's entirely a function of what the employer thinks the needs of his or her employees are.

MR. GRUBBS: When people should be able to retire is a needs related question. People ought to be able to retire when they're not able to work anymore. Of course, they should be able to retire when they're disabled, or when through age they're physically or mentally not able to do the job or a job that's comparable to the sort that they have been doing. But I think many Americans also look forward to retirement as having a point in the latter part of their life when they can relax from active employment. I think that's a good thing. It's a question of at what point can you afford to do that. On the question of when people need to retire, that differs greatly with individuals. Some people in that sense need to retire at 55 and others are able to keep working well into their 80s. But, as a matter of retirement policy, one has to set some age at which you feel a substantial portion of the population is no longer able to work. There's not a right answer to that. I feel that the age 65 is not a bad answer to that in terms of a policy objective. People who want to retire earlier than that should be able to do so at their own expense.

The Social Security Amendments of 1983 made changes that many people referred to as raising the retirement age from 65, stepping it up to age 67. The retirement age was not increased at all. Before this change people could retire at 62. They can still retire at 62. Before the change people could retire at 65 and get bigger benefits than they could get at 62. And before then they could retire later than 65 and get even bigger benefits. Retirement age is only a continuum. After 1983 you can still retire at the same ages as you could retire before, but at any age that you choose to retire you'll get a smaller Social Security benefit than you would have gotten before. It was really a benefit decrease rather than an increase in retirement age.

We have built into the law the idea that people ought to start receiving their benefits by age 70.5 and the idea it's bad to get them before 59.5. There's generally a penalty if you get them before 59.5. I agree with the concept of setting some minimum age for receipt

of benefits under either Social Security or under those programs that are tax favored to provide a retirement income, such as the private pension plan. And as a practical matter you have to set some upper limit under private plans like age 70.5 to prevent tax avoidance, which was what the requirement was designed for. The numbers 59.5 and 70.5 are particularly poorly chosen, because no one knows when his or her half birthday is. In fact, if you were born on July 1, I think we might have considerable difference of opinion about what year you attain age 70.5. If you look at it in terms of months you get one result and if you look at it in terms of days you get another result, neither Congress nor the IRS has told us which one is the right answer yet.

When do you think people ought to retire or when their benefits ought to commence?

MR. ARNOLD: Retirement needs to be defined. Particularly, we see in some occupations where individuals have difficulty in that occupation after they get to a certain age. Maybe age is probably not the right word; fitness level might be better. A policeman or fireman in many cases as he gets older reaches a point where he no longer can perform the functions, and it's really a career change that we're talking about rather than a true retirement from all employment. The negotiations that have gone on between various collective bargaining groups have a great deal to do with what is considered retirement by those individuals and those employers, so that through the various collective bargaining agencies and different industries and different occupations there are different "retirement" ages that have developed and I would think that Congress should not disturb that. It should allow individual occupations, individual circumstances to evolve so that retirement can have flexibility for the industry and for the individuals. As to how much to receive, maybe I'm too brainwashed by the training of the profession, but the concept of maintaining the same standard of living after retirement as enjoyed before retirement, which I think is tied into the three-legged stool concept, still makes some sense to me.

MR. DASKAIS: Don, you mentioned that 65 seems all right. I don't disagree with that, but I would observe that in large companies, including their bargaining unit plans, where the retirement income is pretty high by the standards of other plans and where reasonable early retirement benefits are available, employees do retire at 60 or 61. I believe most of those are truly retirements from the work force rather than retirements to take on a new career. Second, you mentioned the age 59.5. I would suspect that there would be no policy reason for any minimum beginning distribution age if, as Dan McGinn had suggested earlier, all benefits had to be taken in the form of a life income or joint and survivor income. I don't think we would then have short-term investment merely to defer taxes.

MR. JOHN C. MUEHL: I'd like to separate the issue into the privately provided retirement income versus the publicly provided. On the privately provided side I agree with Ken that maximum flexibility should be the key. On the public side Social Security has made a step in the right direction in spreading out the retirement ages. I don't know that 65 is such a magic age anymore. People are living longer, staying healthier longer. They're moving in the right direction in spreading out the retirement ages. What some health insurance people are looking at now that may be applied to Social Security is restricted activities of daily living. The Social Security System is a welfare system and should be based more on needs. It should just be based on when people can't work

anymore. Some health insurers are looking at measures of when people can't take care of themselves anymore. Maybe something like this could be applied to the Social Security system also.

MR. TROY J. PRITCHETT: Age also has to be looked at from an intergenerational point of view. In other words, one side we haven't talked about, which I think is a difference between when ERISA was passed and now, is that the asset side issues become much more important than the benefit side issues. Here's the amount of tax subsidy we're willing to give for these retirement benefits, but then 15 years later that tax subsidy has accumulated a trillion dollars in assets. So now you have to rethink, is that still an appropriate level of subsidy given the fact that these pension funds own 30% of corporate equities and the like? I think if you look at the share of retirement income as a percent of retirees' income, or if you look at the benefit contribution dollars as a percent of the compensation dollar, it's much smaller than the pension fund assets as a share of capital market dollars. Those are issues that we're more used to looking at, what the benefits are rather than the realities of the assets those generate.

I don't think that we as actuaries are very good at the macroeconomic issues relative to the benefit microeconomic issues. In other words, we're very good at saying here's what these policies mean for this plan, but for instance, one thing that hasn't been mentioned is that the biggest thing Congress has done on the retirement income policy is to have a large deficit. If you have a large deficit, interest rates go up for people who have bonds. That means you're increasing retirement income for the people who currently have large savings, many of them older people. If you give a tax break and also at the same time have a fiscal policy that drives up real interest rates, you've done a great thing for the retirement income of current retirees. Well, what does that do to future retirees' income versus what it does to current retirees' income? I think part of the reason we may not be more effective in policy issues is that we concentrate too much on our little share of what the benefit side of the retirement income is, versus the bigger economic reality of how you're dividing up savings or the ownership of the production.

MR. CHARLTON: It seems to me that there should be a relationship between the source of funds and future income and the payment out. We've had a lot of comments about the year 2020 when the ratio between the number of workers and the number of retirees will be 2-1 and seemingly feel that is going to be a bad imbalance between the persons who have to provide and those who are going to receive. In the past, we have had a much higher worker-retiree relationship, and this has allowed us to look to more funds coming in. It seems to me the retirement age should be some kind of balance between the relationship between the people who are going to be putting money into the system and those who are going to be taking out. And so the retirement age probably should advance year after year in order to keep some kind of balance between the stress on the payors and the relief for the payees.

MR. CHARLES A. PEIRCE: I want to support a couple things: one that was mentioned here and a second by the keynote speaker. I think that a national retirement policy ought to recognize the gradual retirement principle as not necessarily a retirement, but a shift in how you operate; i.e., how you allocate time between work and other activities. It makes the retirement concept a little less traumatic, and as you age you

think a little more about those things. The other is something that I wanted to work in some place between the motherhood/three-legged stool discussion and the nitty gritty comments. I wasn't sure where to do it, but a couple of speakers ago the Social Security system was described as a welfare system, so I think this is a good place to bring it in. I have a sense, although not supported by facts, that there may be more an increasing percentage of people not covered by the first leg of the stool, Social Security. Maybe retirement policy (or income replacement) isn't the forum in which to consider welfare people and people who have inadequate Social Security as a result of low covered earnings, but those groups should be recognized when thinking about the policy.

MR. SCHUYLER W. TOMPSON: I happened to have just had my 60th birthday so I'm very sensitive about this subject. My personal opinion is that I really don't have any desire to retire, certainly, in the near future and as long as I can find some way of making money, and buying bread and paying the rent I'm going to be okay. But I want to take the liberty of reading a paragraph of Anna's paper here:

> Early retirement has been a convenient method of dealing with the need to reduce work forces in recent years. It has been economically feasible since the number of older people was not that great compared to the number of younger people. Large companies often favor early retirement and are today willing to offer generous benefits to make early retirement attractive. However, retirement at age 55 or 60 is certainly not necessary on a general basis because of health status, or physical, or mental inability to perform work.

The observation that I would like to make is that it's important to take into account the life expectancy at retirement age, and I think that has to be factored in here, as well as the fact that, of course, the funding period is going to be lengthened. As you postpone retirement, you're extending the funding period. So I think those are two critical items that really will have to be taken into account and, probably, those are items the Senators and people who are not familiar with actuarial subjects need to know; the way these numbers work. I think they'd probably have a hard time dealing with this, so I think we have to be the advisers and act as expert witnesses in areas such as this.

MR. DASKAIS: I believe that the general perception of employers is that older employees are not as valuable as younger employees. Obviously, if you want to reduce the work force and older employees are just as valuable, employers could just lop off at the bottom of the seniority list or whatever substitutes for the seniority list for nonrepresented employees. Also, were it not for this perception we certainly wouldn't need an Age Discrimination in Employment Act or any of the similar state acts. I believe, based on talking to personnel and management people that the employers' perceptions are correct, that is, that the older employees are not as valuable per dollar of pay as the younger employees. That's why we have retirement plans. The first retirement plans, long before ERISA and long before any of us were even alive, were not put in by employers because they were benevolent institutions. They were put in because they wanted to get rid of the old people. That's why we have retirement plans and we shouldn't lose sight of that.

PANEL DISCUSSION

MR. GRUBBS: The question of amounts of retirement income cannot be divorced from retirement age, but let's look at amounts of retirement income more specifically. How much retirement income should be provided and how much of the resources should be spent on the elderly who are no longer employed? I believe that the policy objective should be to assure generally that people can retain a standard of living in retirement like the standard of living they've had just prior to retirement.

We have priorities. We would put a higher priority on assuring that everyone has at least some minimal income, to assure that all older people at least can afford shelter, food and clothing on some minimal level to at least be up to the poverty level. But that by itself is not adequate. Social Security generally accomplishes that objective, but our policy also needs to be to provide a retirement income which is generally adequate to maintain the preretirement living standard.

In terms of allocating resources, if you have a general condition in which individuals are much better off just before retirement than after retirement, you might say we've allocated relatively too much of the resources to the preretirement period; in that case we should allocate less resources to the preretirement period and more to the retirement years. Conversely, if people were much better off in the retired years, one could conclude that they could have lived a little better during the active years. You have a different effect to the extent that benefits are prefunded through savings during the years people are working, than when they're funded on a pay as you go system under which the younger people are now paying for the benefits of those who are already retired.

There have been a number of studies on the amount of income actually needed to keep retirees at the same living standard as before retirement. The President's Commission looked at the question. Tax rates have changed since then, so the numbers change a little bit. It certainly depends upon whether people were married, and their income level and age and other factors, but the number is somewhere around 70%. It's not 100% because of more favorable taxation after age 65 and after retirement and the lesser tax on Social Security during your retirement years.

MR. STEINER: I would say that, with respect to the floor of protection, the current policy is to provide income at a little bit above the poverty level. As long as that's somewhat equitable with the working population, I think the current policy does not have as one of its goals to assure that everyone has the same standard of living after retirement as before retirement. I would see that latter goal as a major shift if that were to become policy. I would not personally like to see that. I like the flexibility that plan sponsors now have to design their total compensation program to meet the needs of the employees rather than what I consider a too paternalistic scenario that you've painted. I think that while it's nice to do the mathematics to develop what the preretirement standard of living is, and we certainly use that a lot to help our plan sponsors design their programs, I think that to require this as a policy of the government would be doing something I would prefer the government not do.

MR. GRUBBS: Several people have talked about our three-legged stool. What do you see as the role of each of these legs and any other legs you care to discuss?

MR. STEINER: I've heard that there are four, or maybe some people in this room can come up with more legs to this stool. The fourth leg is work after retirement, which I think fits in with the comments that a number of people have made. I think that Social Security is, obviously, very important. Something like Social Security with a safety net is important to keep people whole after retirement provided that they've put in a career of working. I view the government sponsored Social Security program as a very important source of retirement income. Privately sponsored plans are also very important, primarily due to the deficiencies that I see of paying for the whole thing out of Social Security. If the entire benefit promise or your maintenance of the standard of living were provided out of Social Security, the costs would go through the roof and we would probably have less savings than we have now, and I just don't perceive much support among the American public for expansion of Social Security above its current level. Privately sponsored plans are very useful tools for the government. The government has as its policy objectives broad coverage and flexibility. With the tax incentives offered to private employers the government cannot insure the policy goals, but it can go a long way toward accomplishing them. This is almost a statement against motherhood itself, but I would be in favor, if I had dollars to spend or if they were my dollars to spend, of not spending them on IRAs but rather on privately sponsored plans. I don't know if Congress has taken the position in stepping back from IRAs, because the tax incentives, the expenditures to encourage individual savings, were too costly relative to the policy benefit derived from those tax expenditures. So I think private individual savings is important, but I would not provide significant incentives for individual savings. I would provide the incentives through tax expenditures for privately sponsored plans.

MR. GRUBBS: Social Security has done a great job in filling that portion of the needs that it has filled of keeping most of the people with broad Social Security coverage out of poverty, and of providing somewhat higher incomes for other people. It falls a long way short of the adequacy goals that I talked about, however. Since people need an adequate retirement income, we have to fill this gap with something. I think the private employer system is the best thing to fill the gap. It does a good job for some people now and it needs to do more. The employee plan should be favored as a policy matter to fill that gap.

We cannot count on individual savings for much for most people and, therefore, I wouldn't invest much public resources in them. To the extent that people save that's a good thing, but I think that history shows that individual savings will benefit such a narrow segment of the population that they don't warrant a very substantial public investment. I would rather spend tax dollars on employer sponsored plans.

What amount of retirement income should be the policy goal, and what should be the roles of various sources in providing it?

MS. SHERRIE B. DESMOND: I think we have demographic issues here that we need to worry about, plus, recent changes in law that we haven't yet felt the effects of. To give you an example, I think we all know people, and we certainly deal with plans, that are more than generous for a career employee, using your 70% as the right kind of retirement income target including Social Security. I think that we probably all deal with pension plans that may provide 50% of pay at retirement for a career employee and

Social Security might add another 30% and we're already over your limit. I certainly have acquaintances, and see many recent retirees, who are saying they're better off than they ever were in their whole lives. But that happens only where we have career employees. We probably all likewise have clients where the average service for each retiree is maybe twelve to fifteen years. And that block of people who had just recently retired probably had no other pension, because they didn't stay long enough in prior employment because they were employed pre-ERISA or needed the ten years. Now, since the 1986 Tax Reform Act we're in a situation where we're going to have lots of people with lots of small pieces of retirement benefits. That's difficult for us to take into account, plus, we all know what inflation does to those old pieces. Perhaps, we need to focus some more on helping those people keep those smaller employer provided voluntary pieces as a part of their retirement savings so that when we get to actual retirement the total employer piece is significant. It may not be if it's only based on the benefit from the last employer.

MR. MUEHL: Social Security provides a good floor of benefits. It's performing its function properly as the welfare system, but I really would back away from any mandatory employer minimum provided pension. Companies are subject to two competing forces. There's competition for employees and for that they want to provide good employee benefits, not just pensions, but all employee benefits. But then there's competition for business, too, and that's a force that drives things the other direction. And the competition for business is no longer just competition with other U.S. companies, it's competition worldwide. And if companies were forced to put in pension plans in the U.S., they might find it easier to go overseas for their help, so that's an issue I think we have to be careful of.

MR. MCGINN: Somebody just mentioned that a great many people may be entitled to many small amounts of retirement benefits because they might have worked for several employers for very short periods of time. Without any mandated indexing of benefits to reflect CPI changes, these benefit values may be quite small and subject to lump-sum cash-outs. However, private plans could be revised to make these numerous small pension benefits far more valuable. For instance, Ontario, Canada, has recently introduced into its private pension system a requirement that vested terminated employee pension benefits be indexed in order to maintain their purchasing power. It seems to me that is something which this country, ultimately, is going to have to face up to. If the many small pension benefits earned by terminating employees were indexed, they could become an important part of an employee's long-term retirement security.

Another factor that should be considered in measuring the adequacy of an individual's retirement income is whether or not such income from one or more pension plans will be sufficient to help the retiree maintain adequate health care coverage. Many employers are terminating their post-retirement health care programs for new retirees. Still, a great many employers also are requiring retirees to pay a progressively higher percentage of the total health care premium during retirement years. Effectively, this latter action requires retirees to pay what is essentially a "cost-of-living" adjusted annuity since the post-retirement self-pay premiums continually escalate with endlessly rising health claim costs. So, it seems, if you consider the "total picture," a retired person's retirement income must be adequate, in addition to being sufficient to pay for food and lodging,

also to pay for the endlessly rising health care cost in retirement years. Solving the problem of providing an adequate retirement income is very complicated because we can no longer just look at the cost of food and lodging during an individual's retired lifetime. We must consider the cost of maintaining proper health care and the cost of adequate food and lodging as a single cost "package."

MR. GRUBBS: Should employer coverage be required or encouraged, and if so, how? I have long been an advocate of the idea that every employer should be required to provide a pension for every employee. This idea of a mandatory universal pension system (MUPS) is not new. It's one that has been in effect in several countries for many years. I introduced the concept in this country in an article in *The Actuary* in 1970, and when the Society held its first specialized meeting, a meeting on pensions in 1972, I was asked to discuss the topic. In 1979, when the President's Commission on Pension Policy was formed, it was reading the article in the *Transactions* from that 1972 meeting that caused the Commission to focus on the idea. So actuaries do get listened to, at least by some. The President's Commission endorsed the concept, though some of the details of its conclusion were different than what I had proposed. I want to describe just what it is I proposed, why I think it's needed, what its cost would be, how it would be administered and what its effects would be.

Every employer could meet its obligation to provide pension benefits under any type of qualified plan, defined benefit or defined contribution. It could be a profit-sharing plan. The employer could instead buy IRAs for its employees. Programs could be insured or trusteed. The whole range of ways of meeting obligations could be used. Alternatively, an employer could elect to contribute directly to a new portable pension fund.

There would be a minimum required level of contributions or benefits. For defined contribution plans I have suggested minimum employer contributions of 3% of pay, and the President's Commission endorsed that idea. I suggested a three-year phase in, 1% the first year, moving up to 3% over three years.

For defined benefit plans, I suggest that the minimum benefit be whatever the accrued benefit would be if one had contributed 3% of pay and accumulated it at some defined rate of interest specified through the law. This is somewhat like a cash balance plan where the accrued benefit is defined in terms of purported contributions, or like the way in which we determine the benefit derived from employee contributions under a contributory plan.

I propose the minimum required benefits or contributions for future service only. As a result this proposal would only gradually alleviate the problem, but it would avoid imposing past service costs, which could be a heavy and unfair burden on employers who already have older, long service employees. While past service benefits would not be required, I would anticipate that, just as now, many employers would indeed provide past service benefits and would provide benefits substantially above the minimum required contributions or benefits.

In order to assure that workers receive benefits for all of their years of employment, I would require immediate and full vesting for these minimum required contributions or

benefits. Any benefits that exceed the minimum required benefits would be subject to the present vesting requirements of the law.

Since my objective is to assure that people receive an adequate retirement income, I would require that the benefits be paid in the form of an annuity payable for life for the individual or the joint lifetimes of the individual and spouse. I would not permit a lump-sum distribution since that would really defeat the basic purpose. Providing 100% immediate vesting produces lots of small benefits. Keeping track of those is, of course, an administrative burden. That's why many employers cash out small benefits. To solve that problem I would establish a federal portable pension fund so that an employer, instead of paying that lump sum to the individual, would transfer the lump sum to the federal portable pension fund. This is no harder than paying the lump sum to the individual. The assets of that federal portable pension fund could be invested through the Federal Employees Thrift Plan. We have an existing vehicle for investing contributions in a federally managed program.

Individuals could have individual accounts in the portable pension plan. After the money was transferred in, it would be treated like an individual account plan, regardless of whether it had come out of a defined benefit or a defined contribution plan. When the worker retires and begins to receive his Social Security pension, this could be an automatic trigger to begin his payment under the portable pension plan by converting his accumulation into an annuity.

The record keeping for the portable pension plan might be handled by Social Security, which already is handling record keeping at a cost of only 1% of the OASDI benefits, remarkably low record keeping costs.

Why is a mandatory universal pension system needed? Because people need an adequate retirement income. Social Security alone doesn't provide it. Individual savings for lower paid people generally do not exist. Lower paid people are having trouble paying the rent and buying the groceries, and no amount of encouragement, exhortation, or tax incentives are going to get those lower paid people to save any substantial amount. The employer plan is an excellent program for those who have it, but many don't. It is because I think that private employer plans are needed and valuable that I have been working in this field for years, and I want to expand those plans.

What would this proposal cost? For an employer with no plan now, it would cost 3% of payroll. If an employer already has a good plan, it might cost nothing at all. An existing program might well satisfy the requirement with little modification. Other employers would have costs somewhere between 0-3% of pay. If an employer already provides a benefit for an employee that costs 3% of pay, for that employee the proposal costs nothing. If an employee is now getting no benefit, it's going to cost 3% of pay to satisfy the minimum requirement.

Where's that additional cost going to come from? It can only come from three places, either reduced profits, or a pass through to higher prices, or lower wages and compensation. We might have differing opinions about the proportion that would come from each of those sources. I think ultimately most of it would come through smaller wage

increases. This country has a long history of wages going up faster than inflation, although irregularly to be sure. Social Security assumes that future real wages will grow at the rate of 1.3% per year. I would allocate a small portion of that to assuring that people have an adequate retirement income.

Would the administrative burden be too great? You would have lots of little pensions, but the ability to transfer that out as a lump sum into the portability fund would not create any great burden. If a plan has an eligibility requirement of age 21 and one year and wants to keep that provision, it could pay the 3% for those not yet eligible directly into the portability fund until they become eligible. For the little employer who thinks that any plan at all would be too much administration, paying 3% to this federal portable pension fund is equivalent to paying a social security tax. This is not an overwhelming administrative burden in my judgment.

What would the effects be? It would greatly expand the private pension movement, extending coverage and increasing contributions. It would generate large amounts of savings which our economy greatly needs to improve productivity. I estimate there would be roughly $50 billion of additional annual savings to be invested by insurance companies, banks and other private sector investors. And most important, it would help assure that every American worker receives an adequate retirement income.

MR. STEINER: We already have a mandatory piece of retirement benefits and that's the Social Security piece. Current policy is to encourage privately sponsored plans through the carrot and the stick approach. While the carrot seems to be getting smaller I think it still works. I perceive that the current incentive, the tax incentive, is still important. I think without the current tax incentive most employers would give up on their plans unless they couldn't, and would just pay their employees more and everybody would be encouraged to save. So I think that the tax incentives are very important. I think that they work and I think, by and large, the system is working fairly adequately.

I think your proposal would increase the cost of labor and I would see employers moving operations to Mexico and this is just the beginning. Three percent sounds reasonable, but next year it will be four and the year after that it will be five, etc. That would be my fear, but I guess holding there would be a fair amount of lost tax revenue from your current proposal. And in the deficit situation, unless you've got some kind of a proposal that would cover the loss of revenues, I don't think that Congress would be real excited about putting in a program now that expands the tax loss.

MR. GRUBBS: Congress won't enact my proposals this year, so there are some things I think we could do to encourage coverage without doing that. In particular, I feel that simplification is something that's greatly needed. We have had coverage, in fact, declining a little bit and many small employers, just overwhelmed with the complexity, terminating plans. We have to grapple with the need for a simplification. I am expecting that efforts in this front will result in an introduction in legislation within the next month or two, which I'm hopeful will have the support needed to make some progress on that front. But complexity is a matter in which we have to fight tooth and nail with every new proposal.

PANEL DISCUSSION

MR. RIAN M. YAFFE: Don, back in 1970, I heard you make that proposal and I'm glad that you're still making it today and that it hasn't become a reality in the last twenty years. I'll tell you I'm just sick and tired of mandates and requirements, and requirements and mandates. I was telling somebody recently that I used to enjoy coming to these actuarial meetings 20 years ago. And I don't think the change is just my age. There was a lot more discussion of this type of subject than the unfortunate session I had to sit through with the Internal Revenue Service. Just look at what's happened regarding the regulatory environment in which we work. I'm sure retirement income isn't the only area that's been subject to that. It's just a horrendous cost. When you think about all the people sitting in that room trying to deal with these totally asinine rules and regulations which have resulted because of Congress' confusing tax policy with retirement income policy, I think the last thing in the world we need is some more additional mandated benefit. I perfectly agree with you about the need for adequate retirement income and so forth and so on. But to do it, getting the government more involved, the idea of a portable government pension fund is about the worst idea I've ever heard. We all know what kinds of games Congress and the administration keep playing with the Social Security fund and those assets. The last thing in the world we need is to give them more assets to play around with.

MR. GRUBBS: Are there any more ringing endorsements out there?

MR. MCGINN: I tend to agree with the last speaker in most respects, but I think that your idea might be possible to implement if we think in terms of using it as a vehicle to start privatizing a segment of the Social Security system, giving the young people a chance to believe that they ultimately will get something out of this program. I think a portion of Social Security taxes might be diverted to individual accounts maintained for the younger members of our covered population. For example, if the Congress, in its wisdom, wanted to give young people confidence that they might have a degree of adequate income in their retirement years, a piece of their contributions already required to be paid under the Social Security system could be paid into an account that would be maintained under a trust where funds would be invested outside of government control by trustees in the private sector. Perhaps some of the dispute between the Administration and Congress concerning use of Social Security "surplus funds" to cover up deficits could be eliminated. Such a technique might be the beginning of a way to start to privatize the Social Security system, to some degree, without increases in taxes while giving young people an opportunity to have confidence that they eventually will receive some Social Security benefits under the federally sponsored retirement system that the Social Security system is supposed to be.

MR. GRUBBS: Dan, let me ask you a question about that. I see the rationale of an individual account system in Social Security, but how do we get from here to there? The current contributions are all needed to pay the current benefits with a rather minor trust balance there. Would we need to get this going by raising the tax level a little bit so we have something to put in those individual accounts?

MR. MCGINN: No. In fact, you just reminded me of what I originally intended to say. Anyone who knows me would have certitude that I probably would never endorse the views of Senator Moynihan, on any subject. However, he has suggested a reduction in

Social Security taxes because of the continually growing Social Security surplus, its use in covering up a growing federal deficit and the difficulty the current tax burden imposes on younger and low-income workers. Perhaps his ideas could be adopted as a "seedling" of a national retirement income policy. Perhaps it would be feasible to carve out some of the monies that are creating the Social Security surplus funds, and use them to form the foundation of a national retirement income policy. Individual accounts for younger workers could be established in a private, mandated retirement program, and that plan would engender some true confidence among young people that they will receive at least a minimal retirement income. The vast bulk of these young people will never save enough money to provide any kind of a retirement income, but this approach could give them a sense that they have a stake in what is being taken out of their pay as Social Security taxes. It could still be designated as a Social Security tax, but this would be a privatized piece of it and an integral part of a national retirement income policy. Perhaps it could be dovetailed with Moynihan's approach to stopping these surplus funds from accumulating and being used to offset the deficit. The limited privatization I mentioned would certainly shut down the rate of increase in the surplus. Ultimately, there would be no surplus since the excess contributions would be invested in the private sector. I'm sure implementing this idea would be very complicated since you have to account for paying benefits to the entire population of retirees. Maybe this diversion of contributions would have to be limited to only a segment of the population, perhaps the younger people. I think the concept is worth exploring and something could be done while avoiding an increase in taxes. There is no politician who wants to be on the front line of saying he's supporting increased taxes. So, I don't think we're going to see the Federal government mandating a private system with a minimum contribution of 3% of compensation: the public would view that as the government creating a new tax while calling it something else simply because the private sector pays it separately.

MR. DASKAIS: I would like to underline something that Don said earlier and that is that the Social Security system in his opinion and, certainly, in mine is working very well now and I don't want to mess with that floor of protection. The question I have for Don is: Is the only difference between your proposal and just increasing, if you will, future service Social Security benefits the investment of the funds accumulated in the private sector? I believe economists would agree that is good, but am I missing something? Is there something else?

MR. MCGINN: Well, you're right. You've hit the crux of the matter.

MR. DASKAIS: I would like to address the complaints about the complexity of our system as exhibited by the session with the IRS and point out two things. First, were it not for the complexity there would be 250 people at this meeting instead of 750, so we are all indirect beneficiaries of the complexity of the system or at least we have relatively highly paid jobs which somebody thinks are very good jobs. But second and more important is that we are certainly responsible for the complexity, because we have responded as true professionals to Dr. Enthoven's (at the General Session) $500,000 a year doctor who comes to us and asks, "How can I defer taxation on as much of this as possible and, by the way, give my assistants as little as possible?" And by doing our job as professionals in the service of a highly paid person, we have created what appears to be the

inequities which, in turn, have caused the Congress to give us top heavy rules and all the other things that we now have.

MR. PRITCHETT: I'd also like to bring up my demographic arguments again, since I'm kind of representing the young person's side. I was paying particular attention to try to see where you said the cost of your plan was going to come from. And since you said, basically, you thought it was going to be lower wages, I interpreted your proposal to mean that lower paid people are, basically, stupid. In other words, they don't maximize their utility, by spending too much now and not saving enough, and we're going to come along in a self-serving manner, since we're private plan administrator people, and make you save this money that you're going to need when you're retired and you'll thank us for it later. I agree with the person who said you could look at this as a mechanism for privatizing Social Security. If you look at the government expenditures as a business rather than as pleasing constituents, I think your analysis will change. In other words, Congress does a good job of what it is currently set up to do. What it is currently set up to do is to please voters, not necessarily please people. First of all, people under 18 don't vote, so there's a constituency that's relatively underrepresented relative to the number of people. Second of all, people who are older and have more money tend to vote more, and the Social Security system does do a good job of pleasing older voters. Young people are often bashed for being our savings problem. In other words, it's those lousy baby boomers. Those are the people who are our savings problem, right? They have all this consumer debt. You know they just don't save for the future. They're short-term oriented, but if you look at the way the government spends its money, which is very short-term oriented, it's old people that have the short-term incentive. In other words, if you look at their future lifetime, it's much shorter relative to younger people. I think younger people, if you believe people are rational, are much more likely to have a long-term perspective than older people. Although they may have less wisdom because they haven't been around as long, if they were rational they would have a longer-term perspective if they don't have a benevolence motive. So our system is not set up to maximize economic growth because of that, in other words, our government expenditures basically please consumers because that's where most of the older voters are. A big problem of our economic growth is that our expenditures go to pay old people's health care. They go to pay Social Security, and they go to pay a lot of retired government pensions and a lot of it goes to the military, which may or may not be a good expenditure. History may prove that it's a good expenditure. In other words, if you can't control the seas, or if you're attacked and your assets are stolen, the trade becomes much more difficult. You can debate whether that's a productive expenditure or not. But I think if we shifted more of our government expenditures to younger people, to education, to training, the infrastructure would improve our economic growth. But I don't really see that that's realistic, because the voting system is just not set up to do that. If you could visualize the thought experiment where people voted the present value of their expected future lifetime and parents voted their children's votes and imagine what that would do to the political spectrum, you might see what economic growth type voting would do.

MR. ARNOLD: I agree somewhat with what the last speaker said and would like to build on some of his comments and the thought of a global economy that we're struggling with. I believe we're in an economic war with Europe, with Asia and with other parts of the world and that war is heating up. If we are too concerned about our

particular problems within the United States, we're going to find that in the long run we'll become irrelevant. I think that we have to look at a larger view, and required programs tend to limit the ability for us to compete. So I think that encouragement makes more sense. Let each individual employer and each individual have the ability to make some decisions. That has worked in the past. I go along with the status quo approach of something which would, therefore, allow us to be competitive in this world economy war we're in.

MR. GRUBBS: We still need to discuss the problems of inflation protection under plans before and after retirement, whether to provide annuities or lump-sum distributions, solving problems of portability, determine what retirement income should be provided to unpaid homemakers, discuss policy regarding favoring defined benefit versus defined contribution plans and determine how pension plans and benefits should be taxed. Ken, since it's possible we might not get through all of those questions is there one of them that you would like to address next?

MR. STEINER: These are policy issues that I have my own personal opinion on, but if any of you feel strongly about issues about Academy involvement or professional involvement in the setting or designing of retirement income policy, I would like your views. If you have a new policy or whatever that you want to propose, I'd read it, but I'm less interested in that. My views and my concerns about actual design of the national retirement income policy are of less concern to me than getting your input in terms of Academy involvement and how actuaries should be involved in the process.

MR. GRUBBS: Should policy favor defined benefit or defined contribution plans?

MR. STEINER: I don't know that there's a compelling reason why policy should favor one or the other. I think there should be a level playing field on that issue, and in general, a defined contribution plan should probably have to provide the same kind of options to the employees as are provided by defined benefit plans. I don't know exactly why defined contribution plans, for example, don't have some of the features the defined benefit plans have.

I'm not sure why the plans shouldn't be forced to provide life annuities or at least go out and buy the life annuities. Other than that I don't see that there necessarily should be any favoring of defined contribution plans or defined benefit plans.

MR. GRUBBS: The issue of defined benefit versus defined contribution plans is very much related to the question of how you're going to make the benefit payout. I'm far less concerned with whether a plan is defined benefit or defined contribution than the question of whether benefits are going to be paid out as an annuity or as a lump-sum distribution. There is far more of a tendency to pay out lump-sum distributions under defined contribution plans. I would rather attack that part of the problem and provide more of an incentive, more of a control for tax favored plans to provide annuities.

This ties into tax policy. Consider an individual who's now age 60 and has just terminated his employment, and has $18,000 of non-pension income that's subject to tax and

therefore is in the 28% tax bracket. This individual has just been told by his employer that he's entitled to a lump-sum distribution or an annuity. The employer said, "You can take a deferred annuity starting at 65; you can take a reduced immediate annuity starting at 60; or you can take a lump-sum distribution." The employee looks at the question and says, well, if I take a deferred annuity I'm going to pay 28% tax on that. If I take an immediate annuity I'm going to pay 28% tax on that. If I take a lump-sum distribution and roll it over into an IRA, whenever I eventually get my money out of the IRA, I'm going to pay 28% tax on that. But if I take a lump-sum distribution and don't preserve it all, then I can use five-year averaging and I would have about 15% tax. We are giving a pretty strong incentive to this person to do what I think is the wrong thing. At least we should do away with that wrong incentive. The way to do it is to end favorable tax treatment for lump-sum distributions.

MR. YAFFE: I have one observation about the defined benefit versus defined contribution question. I see two issues that come up in design. One has to do with the rate of accrual of the benefit, which is usually significantly different in those two kinds of plans, and frequently influences the decision between which kind or on the balance between them. But there's another observation that I think has a more powerful effect in the decision between the two kinds of plans, and I'll just use a 401(k) as a typical defined contribution in these remarks. I have a large bank holding company client that has a defined benefit plan and a 401(k) plan, and its trust department invests the pension plan. It is its own trustee. And in the bank's 401(k) plan, its funds in the trust department are those that are available to the employees. So the difference in investment results between the defined benefit plan and the defined contribution plan is the question of who determines the asset mix, because the equities in both the defined benefit and the 401(k) are invested the same way. Fixed income is invested the same way. And I looked at it over a five-year period through 1989. The defined benefit plan had had an average performance of about 14% compounded, and the defined contribution plan when you looked at the whole fund had had about 9.5% return. So the employees in the defined contribution plan were making the investment mix decisions, and they were being very conservative about it, which I think is what most employees generally do. And yet there was a significant loss of investment opportunity as a result of that. That happens to be one of the factors that makes cash balance plans attractive because the employees are able to get some sort of guaranteed investment return while the assets are available for long-term growth. So I would hate to see a policy that pushed in the direction of one type or another because it could end up being very expensive in the event, for example, the defined contribution plans became favored.

MR. STEINER: I had indicated that I thought there should be a more level playing field. If I can make pretax contributions to a defined contribution plan, then I should be able to make similar contributions to a defined benefit plan.

MR. CHARLTON: On the subject of the weighting towards the benefit plan, the defined benefit or defined contribution, I believe I would favor any emphasis towards the defined benefit plan. At this point, a person who has a personal retirement plan is making the investment in it and investing those funds and is taking the full responsibility. But, in overall retirement policy, aren't we thinking of benefits and the ability of persons to take care of themselves in later life? So the level benefit rather than the funding

method is the important issue. The individual has that responsibility of his own personal retirement plan; but it seems to me that part of this benefit issue should be the providing for the funding not by the employee but by the employer and the investing of those funds by the employer not the employee.

MR. YAFFE: In a certain respect, a lot of what we've been talking about is the question of short-term view versus long term view. In Congress, for example, their long-term view is the number of years till the next election and we're frustrated by that and want to view things to 2020 and beyond. One of the things I've noticed among clients these days is an increasing short-term view. I find them getting out of the business of wanting to make long-term promises to employees. It used to be that the Chief Executive could guarantee long-term employment. Today, the Chief Executive can't even guarantee his own employment, let alone that of any of the employees. Employers are moving in the direction of saying here are the dollars I'll provide you today. Everything is sort of a defined contribution mindset, because when we talk about defined benefit plans or postretirement health insurance 10, 20, 30 years from now, who knows in what form those businesses are going to exist? They're long-term promises that may be just figments of our imagination, and I think the mindset of employers and employees is changing. I think it may have been Dan or someone who said that employees are sort of taking the attitude of becoming more responsible about their future retirement security. They're interested in whether Social Security is going to be there and in what regard. And so I think to some extent trying to develop these long-term approaches is good, and we need to think about it. But I think everybody around us is getting more and more short-term oriented.

MR. DARYLE G. JOHNSON: I want to make just a quick comment about a pet peeve I have in terms of how defined benefit and defined contribution plans are typically named. In the case of defined benefit plans, they're often called "Pension Plan for Employees of the ABC Company" or "ABC Company Retirement Income Plan" or whatever. When it comes to defined contribution plans, they are profit-sharing plans, savings plans, thrift plans, investment plans, incentive savings plans, or whatever and very rarely do you find the name retirement or pension in those kinds of programs. I think it would be very helpful in the case of defined contribution plans if employers were to characterize them as retirement savings plans, or retirement thrift programs, something along those lines. They're just typically not characterized as retirement programs at all.

MR. STEINER: If policy were to favor defined benefit plans and I were a policymaker, given high rates of inflation and investment, I would require some kind of value be given to younger employees. Defined benefit plans are great for older employees, but they don't give much to early leavers in terms of value. A lot of that is due to high levels of inflation and investment return. I don't think this was true some 20 years ago. In terms of value the defined benefit plan gives the younger employee very little. So if I were a policymaker and I went toward favoring defined benefit plans, as part of the carrot, the stick would be either indexing of benefits or, if I were to let people take lump sums, I would restrict the interest rate to use to cash out these people to be even lower.