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EMPLOYEE WELFARE PLANS

1. What are the implications as to the funding of pensions and other benefits arising out of union demands?
2. (*a*) What are the terms of total and permanent disability benefits provided under retirement plans for employees?
   (*b*) What funding methods are used?
   (*c*) What has been the experience as to rates of disability and mortality among disabled lives?
   (*d*) What special administrative problems are encountered?
   (*e*) Can such benefits be provided satisfactorily on a contractual basis?

MR. A. N. GUERTIN stated that "the age of pensions is here." Generations ago a small proportion of socially minded employers made provision through self-insured pension plans, usually unfunded, for the old age of their employees. The unsatisfactory results of this system were followed by the introduction of the group annuity contract and, in turn, by the social security program in the United States.

The American public has become more and more pension-conscious; the desire for security has become of enormous importance in the mind of the average person; and this desire has culminated in a very substantial movement highlighted by the United Mine Workers Welfare Plan, and the recent Ford and steel settlements providing for noncontributory pensions which may well set the pattern of retirement incomes. While these welfare plans involve other benefits, the most important and costly element is pensions. One of the interesting things about the Ford and steel settlements is that they provide for pensions including social security benefits. If this trend continues, the line-up of forces for and against increases in social security benefits may be altered substantially.

There are important implications to the spread of pensions. Should one look to universal pensions for all as the ultimate goal? Must a society be envisioned where an increasing amount of the productive capacity will be siphoned from the producing to the nonproducing portions of the population? If this pressure is directed toward increased social security benefits on a pay-as-you-go basis, the inflationary elements will probably make themselves felt very strongly. Inflation brought about by these elements could be interpreted as the rebellion of the producing portions of the population against the tax load they would have to carry in order to support the nonproducing portions of the population.

The problem to which actuaries might well devote their attention is the

means of finding some way of financing pensions to minimize the impact of this rebellion. This is possible but it would mean financing and funding pensions in ways which would not be very palatable to those who are more interested in current than total cost. To prevent universal pensioning from causing serious economic ills would involve one of the greatest educational undertakings that any professional body such as the Society of Actuaries has ever been called upon to assume. This educational process must permeate employer, employee and public thinking and must demonstrate that the effects of universal pensions involve not only security of promised benefits in terms of dollars but also economic implications so great that they might well change the entire standard of living of the American people.

He stated further that the standard of living of a people over a long period of time is dependent upon the amount of accumulated savings. These accumulated savings, regardless of the value of the dollars in which they are measured, represent wealth in the form of tangible property. This tangible property is an accumulation of what can be broadly characterized as tools. The more tools provided the greater the amount of consumers' goods that can be produced and made available to the public generally, thus raising the standard of living for the population as a whole. If a substantial portion of our production is siphoned off from the producing to the nonproducing parts of our population, the only palliative to inflation is a substantial increase in production. This can come only as a result of savings on the part of the people and the investment of those savings in tools. If the instrument devised to siphon off productive capacity from the producers to nonproducers can also be made the instrument whereby productive capacity will be increased, the standard of living will be permitted to rise or at least not to decline. Fortunately, fully funded plans, such as group annuities and other plans established on a similarly sound actuarial basis, are the ideal savings instrument for doing the double job of guaranteeing the pensions and providing the tools of production necessary to maintain the pensioners after their retirement with the least deterioration in the real value of the pensions.

Whether the channeling of such savings should take the form of equities in industry or merely the advancing of funds to the *entrepreneur* in the form of loans is a question which economists could debate for a long period of time. It is unnecessary to settle that question here, but actuaries will have contributed greatly to the welfare of future generations if they can get across to the American people that universal pensioning is a drag on the standard of living unless it is soundly funded and the funds diverted to productive enterprise.

As one word of caution, the reserve funding of Federally administered public pensions is not advocated. The speaker agrees with members of this Society who have on many occasions expressed themselves as against a funded scheme for social security. But the patterns of pensions cannot be similar for both public enterprise and private enterprise without running into serious consequences. The answer seems to lie in the maintenance of nonfunded public pensions at an extremely low level, certainly not above minimum subsistence, and the building of sound individual pension programs and sound funded schemes through private industry for those who can prevail upon themselves or others to make secure their future.

MR. D. C. BRONSON said that one of the major complications as to funding of pensions and other union demands is the "fissionable" nature of the arrangements. One example is the link to the union agreement and lack of firm knowledge as to what may occur when the agreement comes to an end. Another possible "pop" is the tax treatment by the Bureau of Internal Revenue when some money is going for pensions and some for so-called social insurance. Another potential explosive is the multiplicity of unions in large plants. The unions may be in agreement at the start on a certain program, but later the unanimity may disappear and the original plan be upset.

As to the funding structure, he stated the philosophy of the steel union at present is to keep a little ahead of the funds needed for the pensioners due to retire, possibly providing for those retiring in the next two or three years. This may conflict with the idea that the 6¢ pension contributions are really wage increases. If a plan terminates or an employer goes out of business and all the funding has been applied at the top ages, may not employees say, "Where are those wages that you bargained for back in 1949?"

As a final point on "fissionability," he pointed out that these plans are subject to extra-legal boards set up under the Taft-Hartley Act or by the Administration. These boards may well upset the applecart because they do not give due weight to actuarial facts.

MR. M. H. ALVORD stated he wished to emphasize that there does not seem to be a sound relationship between the benefits promised and the amount of deposits in union-negotiated plans. Although some have a sound relationship, many appear to be developing along other lines. The union first negotiates for the benefit and then negotiates for the amount of deposits for the fund, and there is not necessarily very good actuarial relationship between the two. Likely they hope to increase deposits later on in order to make the plan sound.

He stressed that actuaries can do a great deal to educate the public, the employers and the employees to insist upon soundly financed plans.

In discussing total and permanent disability provisions, MR. E. A. GREEN stated that such benefits on a fully contractual and fully funded basis have not yet become a part of the standard retirement plan pattern. While a demand for such benefits is evidenced by the terms of some welfare funds and by the proposed benefits for total and permanent disability under the Social Security Act, the fact that the cost of providing such benefits is indeterminate and high has deterred many employers from incorporating them in their over-all employee benefit plans. The term "employee benefit plan" is used, rather than "retirement plan," as there is real question whether total and permanent disability income is more closely allied to weekly indemnity accident and sickness coverage than to pension coverage. For instance, the problems of recoveries, occupational *vs.* nonoccupational disabilities, the determination of valid claims, are all present in total and permanent disability coverage. The short waiting period and full immediate coverage provided under accident and sickness plans, rather than the longer waiting period and gradual accumulation of benefits under retirement plans, seem to be more appropriate if the total and permanent coverage is to accomplish its full social purpose. On the other hand, once a claim has been established the amount and type of liability is more nearly akin to that under a retirement plan. The potential liability is large and may extend over a long period of years. At present, most total and permanent disability income provisions in employee benefit plans have been associated more or less formally with retirement plans.

While the need for earlier retirement, usually in event of disability, has been recognized in the standard Group Annuity contract by a provision for earlier optional retirement, usually within ten years of the normal retirement date, this provision rarely provides adequate disability pensions since it allows only for annuity credits purchased to date of disability discounted to the actuarial equivalent at the younger retirement age. His company has issued a few Group Annuity contracts which give the employer the right to buy a temporary annuity from the date of earlier retirement to the normal retirement date, with payments equal to those for the pension credits already purchased which will begin at the normal retirement date, thereby avoiding the necessity of discounting these latter payments to their actuarial equivalent for the earlier retirement date. In general, there is a fairly long service requirement for the purchase of such an annuity and its purchase is confined to a limited period prior to the normal retirement age. No attempt is made to define total and permanent

disability contractually, but provision is made for the purchase of the temporary annuity "if the employee is unable to work, as determined by the employer." There is no provision for advance funding of these temporary annuities, but they are purchased with a single premium at the time the disabled employee retires. It is possible that the cost of these earlier retirements due to disability could be funded through a supplemental deposit administration plan. However, any valuation of this supplemental fund would be very approximate at best and would involve no guarantee as to adequacy due to the indeterminate nature of the risk.

Temporary annuities purchased in this way for earlier disability retirements have not caused any major administrative difficulties to the insurer. The combined service and age requirements tend to keep recoveries to a minimum. The employer has the problem of adequately determining who is eligible for such annuities so as to be nondiscriminatory and still keep his costs within reasonable limits.

The speaker asserted that all actuaries should be seriously concerned with providing a means of filling the hiatus between the weekly indemnity accident and sickness benefits and retirement benefits. However, unless and until a definition of total and permanent disability, meaning the same thing to covered employees, the employers, the insurers, the courts and the juries, can be determined, such benefits will probably of necessity be on a more or less flexible basis rather than fully contractual and fully founded.

MR. C. H. TOOKEY said that he felt the type of permanent total disability benefit which should be provided in a retirement plan should be insurance rather than an integral part of the pension. When the disability income is closely related to the pension formula, there will be a tendency for the benefits to approach one another at age 55 and later. This is a direct invitation to the employer to retire inefficient employees on disability at an age when they should be on the regular early retirement option. Disability benefits should not be paid after normal retirement age, at which time the regular pension plan should take over.

In one large case his company's group annuity disability benefit was $50 per month with a 20-month waiting period because the gift group life insurance provided approximately $50 per month for the first 20 months of disability. This benefit was on a contractual basis, and the experience over fifteen years indicates that the Class 3 table adjusted for the longer waiting period gave a more than adequate premium. His company has also written some total permanent disability benefits both as part of California U. C. D. plans and as supplements to ordinary loss-of-time disability policies. In both cases the experience has been very close to that anticipated

by the Class 3 table. So long as the amounts of indemnity are such that there is a minimum of incentive to malingering, it would appear that normal group underwriting will give a normal disability experience. For that reason it appears that disability benefits can be provided on a contractual basis at a premium determined in advance. In such event there should be no unusual problems either in funding or in administration.

There is at present considerable interest in deposit administration annuities. The question arises as to whether disability annuities should be provided by a contractual premium or charged to the deposit account. He has recommended the former practice feeling that, because there is such a wide variation in the annuity values of various total permanent disability cases, it might be difficult to explain to an employer why the account was charged an average rate for the annuity, whereas under the insurance risk the transaction is one where only the contractual premium is of interest to the employer. If the annuity value for a disabled life is set fairly high, the employer will be reluctant to have a seriously disabled life charged to the account, but he may be very willing to certify disability for some employee he wishes to get off his hands without paying the full retirement cost.

At present there are not many insured retirement plans which do a good job for the disabled employee. In view of the recent social security arguments that only the Government can provide for the totally permanently disabled, it might be well for actuaries to give greater study to this problem. There is no reason why this coverage cannot be provided by insurance companies either in connection with retirement plans or as separate coverage on the group basis. There is available a fairly reliable experience of the cost of total permanent disability in connection with group life insurance, which, together with the Class 3 experience, should provide a sound basis for adequate total and permanent disability coverage.

MR. C. T. FOSTER questioned whether the cost of disability benefits is as high as some may feel. If disability benefits are granted after age 55 and thirty years of employment, there are not going to be too many disabled people and much of the cost will be funded on the assumption of normal service retirements. Of course, if adequate discounts for disability as well as withdrawals are made, a realistic cost for service pensions will be obtained, and then disability pensions will be an entirely additional cost. Probably that is the basis considered by the employer when he thinks about disability costs, but actually the additional costs for this type of disability benefit when one is already funding service pension costs are not too great.

He also suggested that disability factors, rather than the construction

of a service table based on withdrawal and disability, be used in discounting service pension costs on account of disability.

As for past service funding of pensions, Mr. Foster pointed out that the only variable in union plans along the Ford lines is the amount of pension depending upon length of service and only up to thirty years. If pensions do not increase after thirty years, it is probably unnecessary to consider that they accrue over the entire working lifetime of the employee. The benefits might be considered to accrue over the first thirty years of employment, or possibly over the last thirty years. If it is done over the first thirty years, the trust fund or deposit administration contributions are probably larger than necessary because the withdrawal assumption is likely to contain a conservative item. This can be avoided by funding over the last thirty years when withdrawal is not so important, but there is a danger in that procedure of underfunding if the bargaining agreement allows early retirement with full benefits at 55 with thirty years of service but the benefits are not accrued until later years up to 65.

He said that employers in recent months are getting quite a different attitude toward pension plans. Formerly they were quite willing to look at past service funding realistically and actuarially, but now they are inclined to wonder whether there is sense in such action. Perhaps they would do better to get away with the very minimum contributions, as unions may not agree to later reductions in their funding. There is also no assurance that pension plans subject to short term bargaining agreements will continue in effect, so there will be no point in having large reserves built up at the expiration of the agreement. Again, if social security is increased, liability will be reduced and large past service reserves will be unnecessary or else such reserves may suggest that benefits should be increased. This may not be a very healthy attitude but is a practical one and one that many businessmen are following at this time.