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PENSION PLANS—PROVISIONS FOR TERMINATION OF PLAN

DORRANCE C. BRONSON

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RAY M. PETERSON:

Mr. Bronson has again placed us in his debt by this paper in which he very skillfully focuses our attention upon the problems of terminated pension plans.

He opens his paper with the following statement: "The essence of the reserve concept . . . lies in a running presumption that the plan may terminate. . . ." This is an excellent and laudable ideal; however, many of the problems, particularly of inadequacy upon termination, stem from the fact that funding assumptions and practices are often adopted with only a going concern in mind. There is an implicit, if not explicit, reliance upon the employer's continued existence. Relaxed actuarial assumptions and long-term accrued liability funding practices, even in perpetuity, are used. All too frequently one encounters an attitude of letting future management worry about funding inadequacies. There may be entirely legitimate reasons for business management to take this "going concern" attitude toward its pension funding; but the actuary has a responsibility for making certain that business management fully understands its implications and even for encouraging and recommending prudent funding practices.

It is significant that there are few, if any, termination problems where an insurance contract is used. The responsibility which the insurance company assumes *at the outset* assures a careful study of termination features. Employee equities are clearly determinable and do not depend upon actuarial judgments to be formed at some time in the future. Deposit administration contracts may have some of the weaknesses of trusteed plans in resolving equities upon termination, but there is usually an existing actuarial framework of annuity rates to serve as a guide. Critics of insured plans frequently say that the vaunted guarantees of an insurance contract are of value only upon termination of a plan or contract. It should be remembered that by reason of the guarantees assumed by the insurance company at the inception of a plan, a highly responsible attitude in the very nature of things is taken toward funding adequacy.

This funding discipline is of great value to the employer—a discipline which assures that funding adequacy is achieved during the active term of the plan and that there will be no great problems of resolving equities or of assuring the payment of accrued benefits upon termination of a plan.

In Mr. Bronson's Exhibits 6 through 9, the reader must be struck by the recurring expressions "actuarial values," "actuarial equivalents," "as determined by the Actuary," "the Actuary shall compute the actuarial value," "assets shall be allocated by the Actuary," and so on. The author suggests, "Perhaps, we should begin getting ready for the actuarial and other technical problems of such mergers and terminations as will come our way." The importance of the responsibility which the actuary may have in determining equities upon termination of a trusteed plan and some deposit administration plans cannot be overemphasized. The dollar benefits to be received by many ex-employees will depend upon the sole judgment of the actuary for, as we all know, actuarial computations are merely judgments expressed in figures. So long as a plan is in operation, the benefit formula establishes the amount of benefit. For the insurance company contract, the terms of the contract usually determine what is to be received. If two or more actuaries are engaged to determine the respective employee interests upon termination and each has a different answer (which they will almost inevitably have if they work independently), which is the right answer? Are there possibilities of litigation in which the actuary may become ensnarled? The actuary may be called upon to have an order of wisdom exceeding that of Solomon, for a pension (unlike a baby) *can* be cut in two and each part survive!

One important phase of winding up a pension plan, particularly where the employer is bankrupt, is the standing of the interests of pensioners and active employees in relation to that of other creditors. Will legal technicalities be overridden by moral obligations in the public interest? Will legal safeguards become impaired by practices or assurances to employees that have not been clearly qualified? In other words, will the employee have been expected to read all the fine print?

Will the current investigation of welfare and pension funds turn its attention to termination provisions—perhaps stimulated by Mr. Bronson's paper—and will there be some governmental requirements that will provide greater protection to employees upon termination of a plan with respect to benefits which the employees have been led to believe were being funded for them?

Mr. Bronson has stimulated all of us to a new alertness toward the termination provisions of pension plans. If further invasion of the pension field by government is to be forestalled, private pension plans must demonstrate that they are doing not only a good job during the employer's continued existence but also a good job as to accrued benefits upon cessation of the employer's existence without increasing the public burden.

JAMES A. ATTWOOD:

I should like to make a few remarks based upon experience which I obtained in military service while reviewing pension plans for cost purposes under Government contracts. During this period of military service I had occasion to run into many instances of the type of situation which Mr. Bronson would refer to, I think, as a termination of pension plan by reason of business necessity.

This type of termination was encountered under situations where an employer was engaged exclusively, or nearly so, in production under Government contracts. If the Government decides that the employer is no longer to be continued for such production—and this has happened in a number of very clear examples—the employer may be forced to discontinue his pension plan. Concurrent with such discontinuance there may be substantial reduction in personnel and the question of disposition of large sums of money paid in for pensions during the period of Government contracting is raised.

Some pension plans specifically state that funds remaining at termination of plan be distributed to remaining employees. It may happen that under a pension plan for one of these relatively unstable organizations only one or two employees may be left at the termination of the plan for whom huge sums of money are to be applied. Such situations raise questions as to the legal effect of the pension plan and the relationship of the insurance company, trustee or employer to these one or two employees. I can recall four specific examples of the four types of pension plans described by Mr. Bronson where this problem has arisen.

To prevent the dilemma occasioned by such a situation, Government contracting personnel attempted to incorporate in the pension plans, and in the documents which support the plans, a type of termination provision which Mr. Bronson refers to as an indefinite or general provision. Such provision might distribute sums remaining at termination of the plan on a basis agreed upon between the insurance company and the employer or the trustee and the employer in a manner which does not contravene the regulations of the Internal Revenue Code. In some situations specific provisions were made to permit the trustee or insurance company to make a payment to the U.S. Treasury Department of any excess funds at termination. These plan provisions were acceptable to the Internal Revenue Service in the situations used.

I mention these experiences in order to indicate that there are situations where the indefinite or general provisions on termination appear to be preferable to specific termination provisions. If the plan specifically provides that remaining sums be applied to provide benefits for remaining employees, it may be difficult to do otherwise because of the legal effect on employee rights. I am aware of two cases now under negotiation where sizable sums of money are available for reversion to the Government in situations where all parties seem to feel that the money should revert to the Government. Because of employee rights involved and because of the specific pension plan provisions the disposition of these funds is being held up and may even be subject to litigation.

J. PERHAM STANLEY:

Within the past year the UAW-CIO has had occasion to be concerned with the termination of half a dozen pension plans having termination clauses akin to Mr. Bronson's Exhibit 8 clause. This type of clause is probably the most common one in the automotive parts industry. Normally, it differs somewhat from the particular example quoted by Mr. Bronson, in that an additional priority group covering employees aged 50 to 60 on the date of termination is included, and the remainder group (those under age 50) is treated on a deferred annuity rather than a lump sum cash settlement basis. However, the use of the words "without reference to the order in which they shall reach age 65" in the text is common to all of the clauses of this general type.

As a practical matter we have had, to date, no problem whatever arising out of the use of this particular phrase. Its intent was to convey the idea that each individual employee within a particular priority category would have an equal a priori claim, at date of plan termination, to a deferred pension based on his accumulated credited service. No discrimination based on age would be made within any particular category. It is not necessary to wait until all members of a category have reached age 65, because the allocation of the trust fund assets takes place as of the date of termination of the Plan—each employee in categories (*d*) and below being credited with a pure deferred annuity without refund in the event of death prior to 65.

If the trust were continued in being, deaths before 65 would indeed create a problem. So would interest and mortality gains (or losses) over those assumed in making the original allocation—or dividends, in the case of an insured Deposit Administration group annuity—as the Trustee would have difficulty in knowing just how to allocate such gains or losses. Again as a practical matter, however, the administrators of such funds are generally most unwilling to continue the Trust on a closed basis after termination of a Pension Plan. For a variety of reasons, the usual practice is to close out the trust with the purchase of a single premium group annuity, which will provide immediate annuities for some and pure deferred annuities without refund for the rest, and which will be nonparticipating in order to eliminate the problem of allocating dividends.

The matter of how best to allocate gains and losses occurring under closed trusts which might be continued to extinction after termination of a pension plan might well form the subject of an entire paper by Mr. Bronson.

W. RULON WILLIAMSON:

Mr. Bronson's paper on Provisions for Termination of Pension Plans suggests a similar analysis in relation to the termination of Old-Age and Survivors Insurance. There is provision for such termination in Section 1104 of the Act. Under the caption "Reservation of Power," it provides: "The right to alter, amend, or repeal any provision of this Act is hereby reserved to the Congress."

Mr. Bronson's Table 1, with 9 classifications, suggests a series of priorities in event of winding up. He lists them by order of imminence of pension payment, but shows that this is not necessarily the order of rights at such a time. Were the Congress to wind up OASI—with its skimpy funding—it would find that there was not enough in the reserve or trust fund to meet the liability for those actually in receipt of benefits, to say nothing about those called "eligible to retire" but persisting in earning too much money, or the widows whose mother's pensions are over, but who are potential aged widows. Since it seems to me that 1956 might very well pay out more in benefits than is taken in in taxes, I am convinced that one reason for the anxiety to add much greater liabilities in the 1955 Amendments was to bring in more taxes, before this cash deficiency showed up.

The full effect of each build-up in OASI is dampened by the two-year delay before anyone can qualify for the maximum, and well before that times comes, another damper is established. With Mr. Bronson's sobering suggestion of awkwardness in terminating when the cash margin is thin, it would be advisable before more complicating extensions take place that a couple more years of observation should be accorded the wearing off of the lags inherent in the 1954 Amendments.

Pertinent information was adduced in the the Curtis Hearings, where the money-flow was studied—evidence that we were getting in very deep, evidence that was not exactly laughed off in 1954 but just silently shrugged off.

Given *Actuarial Study No. 43*, now at the printers, and *Nos. 41* and *42*, only recently published, assigning the priority to those now on the beneficiary rolls, there would be no equity for those sometimes referred to as numbering 100,000,000, whose contributions—or taxes—have all been spent for the other fellow, and who could have no earmarked equity whatever in a winding-up. If, further, the suggestions of *Actuarial Study 37* and *43* that priority be given to current risks for death benefits were accepted, there wouldn't yet have been any residue beyond the death benefits for an incipient asset-share to aid the potential aged, from the contributions of the "covered."

Some cool accounting analysis at this time might well curb the more demagogic claims of the expansionists. I suggest to Mr. Myers and his assistants that Mr. Bronson's example be seriously followed out.

WILLIAM W. FELLERS:

Mr. Bronson first gave me a preliminary draft of his paper concerning the provisions for termination of pension plans just as I was leaving for a bargaining table discussion of a pension plan that was being terminated, so I was probably one of the first to benefit from the ideas expressed in his paper. My discussion will be confined to some of the problems and solutions found in connection with the termination of the trust fund type of pension plan which has involved some sort of union negotiation. As Mr. Bronson suggested in the early part of his paper, certain points which appear to be trivial may actually become the basis for the decisions finally made. Hence, I am glad that his paper did not ignore the possibility of these trivia, for in the case examples which follow I think you will see how the controlling point has been in this category, even to the extent that it may not be mentioned in the union agreement, plan itself, or implementing funding arrangement.

Case A.—This is the problem of a Company which established a Plan in 1946 covering all employees after they met certain age and eligibility requirements. The Plan provided for a benefit based on $1\frac{1}{4}\%$ of earnings for each year of service while an employee was covered by the Plan, and the Company paid for all benefits (*i.e.*, employees did not contribute). In 1949, after the Fact Finding Board appointed by the President for the Steel Industry made its report, the Union reached an agreement with the Company to establish a Plan such that the net cost thereof would be 6 cents per hour on the basis of a study to be made as set out in the following paragraph taken from the 1949 Supplemental Agreement with the Union.

The Company and the Union agree to institute immediately a joint study of pensions, as recommended by the Board, such study to be concluded on or before March 1, 1950. An amended pension plan shall be agreed upon between the parties and placed in operation not later than May 1, 1950. Such amended plan shall be non-contributory and shall conform to the recommendations of the Board and the requirements of Sec. 165(a) of the Internal Revenue Code (26 U.S.C. Sec. 165(a)) and the Treasury Regulations issued thereunder, and shall provide that employees retiring after April 30, 1950, shall receive, in lieu of benefits prescribed by the present plan, such benefits as may be prescribed by the amended plan.

The following points might therefore be noted in connection with the solution reached in Case A.

1. The termination provision of the Plan established in 1946 was, in effect, by-passed by the language of the 1949 Supplemental Agreement. Note that since benefits under the Plan *to be* established as of March 1, 1950 were to be *in lieu* of benefits under the then present Plan, the union employees thereby appear to have renounced any right they may have had to assets held in trust for the 1946 Plan.

2. Because of this, no assets were transferred from the trust fund implementing the 1946 Plan to the trust fund established for the union employees. This meant that there was a considerable reversion of assets to the 1946 Plan, to the extent that such assets had been accumulated in respect of liabilities for union employees who were pulling out.

Case B.—This is the case of a Company having one Plan covering union employees and another Plan covering the nonunion employees. Separate funds implement the two Plans. One division of the Company was to be closed down, and a considerable number of the union employees covered under the union Plan would thereby be terminated. The termination clause in the union Plan was very similar to that set forth by Mr. Bronson in Exhibit 7*a*, in which a definite order of priority for the assets is established: first for those retired, next for those eligible to retire, then for those eligible for early retirement, and finally for the rest. Note, however, that this situation involved what might be called a "partial termination" of the Plan, since only one group of employees was being terminated, and the termination provision did not make any proviso for such a partial termination. Therefore, we suggested that if the termination clause of the Plan were to be followed, some agreement would first have to be reached on the segregation of assets, and we suggested a number of methods that might be used. The solution of this partial termination by-passed the clause for full termination entirely. It was found from the controlling labor agreement that these employees had unlimited seniority (because the plant was being closed) and so would be eligible for retirement subject to the completion of the age, service and other conditions provided in the

Plan. The solution involved continuing these terminated employees under the Plan and so represented 100% vesting for this group of employees on the basis of their service at the date of termination. It was felt by the Company that it would be better to handle it in this way, rather than to try to have the termination provision amended in any way.

The pertinent points to be noted in connection with this solution are then as follows:

1. The termination provision of the Plan was not used.

2. The employees involved received 100% vesting of benefits based on their credited service, and this point will have to be watched if the level of benefits under the plan is amended upward any time in the future.

3. The cost of providing this 100% vested benefit based on credited service to the date of termination was estimated to be small in relation to the total requisite contribution level. However, such a precedent could be extremely costly in the long run.

4. The Company decided that it would rather pay the price of the 100% vesting for these terminated employees than take up the problem of rewording the termination provision of the Plan or reaching some supplementary agreement concerning the appropriate allocation of assets in the case of this partial termination.

Case C.—This is the case of a Company having a separate plan for employees in each local union, and the problem (simplified somewhat) arises in connection with the termination of one division involving one local. The language of the agreement covering the Plan being terminated is of the sort set forth in Exhibit 8 of the paper, which Mr. Bronson suggests may be of the "delayed priority" type since the allocations are to be made "without reference to the order in which they shall have reached age 65." However, for this case there was also the following paragraph in the agreement in lieu of Sections 2 and 3 of Exhibit 8.

> Such allocation shall be accomplished at the election of the Board of Administration through either (i) continuance of the Pension Fund or a new Trust Fund, or (ii) purchase of insurance annuity contracts; provided, however, that no change shall be effected in the order of precedence and basis for allocation above established, without the unanimous consent of the Board of Administration.

On the basis of the above paragraph, read in conjunction with the order of priorities established by Exhibit 8 Section 1 language, it was decided to use the assets to purchase paid-up annuity policies.

A number of pertinent points that may be noted in connection with this Case C are as follows:

1. The termination provision was followed, and the "without reference

to the order in which they shall have reached age 65" clause was considered resolved by "unanimous consent of the Board of Administration" of the above quoted paragraph, since this "without reference" clause was interpreted to mean that you did not have to wait until all employees reached age 65 for the purpose of final asset allocation. This latter is the exact opposite of the literal interpretation suggested by Mr. Bronson, yet that may have been the reason for its inclusion in the Plan.

2. There were certain other factors considered in the bargaining sessions relating to the termination, and these factors were more controlling legalwise and dollarwise than the termination provision itself. One factor was an agreement by the Company to provide paid-up life insurance to retired employees, and so the Company held to the position that only those employees who actually retired prior to the date of termination of the Plan were eligible for such paid-up insurance benefits. Another factor was the agreement by the Company to provide severance benefits for employees who did not receive any pension benefit, and the question was raised about whether employees receiving an equity in the terminated Plan would be eligible for such severance benefits.

3. The Plan generally provided for benefits subject to the completion of 10 years of service and certain age requirements. However, the termination provision does not mention any service requirements. One possible interpretation would have been to exclude all employees from consideration who did not meet the minimum service requirements as of the date of termination, and another possible interpretation would have been to exclude only those employees from consideration who would not meet such service requirements on the basis of a full year of credit for eligibility purposes in respect of each *future* year until meeting the requisite age requirement. However, there did not appear to be much question but that the level of pension benefits should be related to just those service credits at the date of termination, and this meant that under the second interpretation there would be employees with relatively small benefit credits involved. Hence, the first interpretation limiting consideration to just those employees with the minimum requisite period of service when the Plan terminated would appear to be more reasonable. In spite of this, the other interpretation, I understand, was used in finally resolving the termination of the Plan in Case C. (However, I know of another case involving a similar termination which excluded from consideration any employees with less than the minimum requisite service credit as of the date the Plan was terminated.)

Although the relatively few cases indicated here would hardly provide a basis for any generalizations, the problems raised by these examples of termination pose some rather interesting basic questions, three of which may be noted as follows:

1. Should *all* employees be included in one Plan, or is it better to have separate Plans for union and nonunion categories? (See Case A.)

2. Should *all* union employees be included in one Plan, or is it better to have separate union Plans for separate bargaining groups? (See Case B.)

3. Should service credits to date of termination be used as the basis for determining which employees should be considered for benefits, or should some consideration also be given to future service credits the employees could have obtained if the Plan had not terminated? (See Case C.)

In determining the liabilities at the time a Plan is terminated, Mr. Bronson suggests that the single premium approach is probably the most logical basis and then also suggests that the assets under a fully funded Plan may be in excess of such single premium requirements when a higher class[1] of funding is used. Let us consider this from the standpoint of a person of attained age 45, who entered a Plan at attained age 40 when it was first initiated (but who was employed when he was age 32). If the prospective pension payable from age 65 is \$2.00 per month per year of service, then he would be entitled to receive a pension of \$66.00 per month (based on 33 years of service between age 32 and age 65) and the amount of pension accrued at age 45 would be \$26.00 (based on 13 years of service between age 32 and 45). Hence, by the 1937 Standard Annuity Table and $2\frac{1}{2}\%$ interest the following amounts may be derived by the various indicated methods of funding:

Method*	Accrued Liability	"Normal" Cost
1. Single Premium..........	\$1,649†	\$127†
2. Entry Age Normal Cost...	2,184‡	137‡
3. Individual Level Annual..	1,142§	208§

* As set forth in paper by Charles L. Trowbridge *TSA* IV, 20 ff.

† Accrued liability is the single premium value for \$26.00 per month payable from age 65, and the "normal" cost is the single premium value for one year's credit of \$2.00 per month payable from age 65.

‡ Accrued liability is the present value of future benefit of \$66.00 per month payable from age 65 less the present value of future "normal" cost amounts representing the level annual premium for the benefit on the basis of an entry age 32.

§ The accrued liability represents the present value of future benefits of \$66.00 per month payable from age 65 less the present value of future "normal" cost amounts representing the level annual premium for the benefit on the basis of age 40 when the Plan was initiated.

[1] As set forth in paper by Charles L. Trowbridge *TSA* IV, 20 ff.

It is of interest to consider these figures in the light of a Plan's termination provision and the various funding methods that might be used, bearing in mind that such consideration may be equally applicable in the valuation of prospective pensions payable to a group of employees. Some of the points that might be noted are as follows:

1. The accrued liability by the entry-age-normal-cost method is in excess of the accrued liability by the single premium method. In fact, we see that the accrued liability by the single premium method is only 75% of the accrued liability by the entry-age-normal-cost method, so that a Plan being funded by the entry-age-normal-cost method on the basis of a group of employees with age characteristics like our example may need to have only some 75% of the other type of liabilities for nonretired employees met to be fully funded by the single premium method.

2. On the other hand, the accrued liability by the level annual premium method is only some 70% of the accrued liability by the single premium method for our example. This could mean that the fully funded Plan on a level annual premium basis could be less than fully funded by the single premium method criterion. Of course, this would probably only hold for a period of time immediately following the initiation of the Plan (possibly until the initial eligible group had retired), for ultimately the level annual premium method would involve an accrued liability identical to that of the entry-age-normal method.

3. Since the use of a particular funding method may result in funds higher or lower than the accrued liability by the single premium method, instead of thinking in terms of the single premium method as *the* method for termination purposes, it may also be appropriate at times to think in terms of the funding method being used, whatever method it may be. For example, by the entry-age-normal method, the accrued liabilities may be determined for each employee, and the proportion thereof funded may be determined, with the result being used as the amount to provide the benefits. In other words, what would be first established by this procedure would be the allocated portion of the trust fund assets to use as the amount to purchase benefits for each individual involved; whereas by the single premium approach suggested by Mr. Bronson, what is first determined is the amount of accrued benefits and then the single premiums for these benefits would be used as the basis for the allocation. This approach of first determining what assets are available is, of course, suggested by Mr. Bronson in connection with the allocation of assets when there is a dissociation of groups. The point I am making is that the asset allocations may be done on an individual basis and so may be another possibility for

defining the amounts of benefits to be provided to certain classes of participants when a plan is terminated.

Fortunately we have not yet had much experience with Plan terminations, and I am in hopes that we will have relatively little experience in the future on this score. However, for the cases that terminate we do need to know what can be involved, not only from the standpoint of the actuarial considerations of defining benefits by one method or another, but from the standpoint of the legalities that may be involved in the termination clause as well as in the "trivia" that may actually control. I want to thank Mr. Bronson for his paper which has helped me greatly in my consideration of these termination problems.

D'ALTON S. RUDD:

Quite recently our group annuity business started expanding and we are considering printing a contract. Past service provisions give me pause, even though Mr. Bronson, in his paper, indicates the group annuity provisions as being rather equitable when the usual seniority provisions are used on termination, namely that whatever has been purchased is vested and that should work out.

However, the London Life Insurance Company without having a large number of policies in force, unlike the Equitable, still has some terminations.

We recently had a case of an employer who suspended past service payments and, though most of the people who had their past service purchased were owners of the business, they did request that we reapportion all the past service money which had been paid amongst the remaining employees who were entitled to past service, and this we did on the basis of reserves on the premium basis.

On another contract the employees bought the business. The owner of the business, who was not a proprietor, but who held a large majority of the stock prior to the sale, was number one in seniority and of the six past service annual installments that had been made out of a total of ten required, five and three-quarters had been applied on his certificate.

Now, in Canada we do not have a regulation similar to the American provision whereby, I believe, the benefits must be reallocated if the higher paid employees are benefited too much on termination of employment. Because of this particular example which we have had, I suggest that perhaps group annuity contracts, in Canada at least, should have some reference to reallocation of past service money on termination of the contract.

(AUTHOR'S REVIEW OF DISCUSSION)

DORRANCE C. BRONSON:

An opinion expressed on one of the informal topics at the Montreal meeting was to the effect that the issue of the *Transactions* covering the second spring meeting usually gets in our hands too late to afford much time for preparation of discussions on the papers presented at that meeting. Having been thwarted by this time element once or twice myself, I am especially grateful to those who overcame this handicap and gave us their interesting comments on my paper. I should like to reply briefly to these discussions.

Mr. Peterson, by nature, is inclined to overly underscore my description of the "built-in" termination provisions of the traditional types of insured contracts used for pension purposes. He points out that these are "disciplined premium" structures and not predicated upon the employer's continued existence, or on future actuarial judgment, for the full funding of accrued pensions. But is discipline always good? If an employer is faced with premiums he cannot meet without serious harm to his business, would it not be adverse to the over-all interests of his employees to scrape the barrel for this purpose? Furthermore, as Mr. Peterson surely knows, insured plans do not fully enforce this discipline. Certain "stop-and-go" flexibility is possible for individual contract and group permanent plans and certain devices are available in group annuities—suspension periods and omission of past service contributions. But, even so, the greater suppleness of deposit administration and trust fund plans in this regard is more realistic, including the "split-funding" type which at least one company, with which Mr. Peterson is familiar, is actively promoting.

As for the difference between the deposit administration and the trust fund in connection with resolving equities for nonretired employees, I see no particular advantage in Mr. Peterson's reference to a framework of annuity rates in the deposit administration contract. What counts at time of termination is the size of the fund, and for identical plans a deposit administration could be practically void of funds and the trust fund well-heeled, or vice versa. Premium rates would be applicable only in dividing up what was there, and it seems to me the actuary's rate basis under a trust fund plan would do at least as well for this purpose as the premium table in the deposit administration contract.

Coming to his point on the possible conflict of actuarial opinion, isn't this a natural phenomenon in any profession? It seems to me I have heard rumors of actuarial disagreement even within the walls of a single insurance company. Litigation involving actuaries is possible; it always has been possible. But let us consider ways of minimizing it; it won't be solved by claiming that, since a clear-cut termination clause can be found in an insured contract, that method is the only proper medium for funding pension plans; this would be the tail wagging the dog. Admitting the existence of several types of plans, let them all do a better job of clarifying the equities and procedures in case of termination.

On Mr. Peterson's interesting point as to the standing of the pension interests relative to other creditors, it seems to me that if the employer has made no pension commitments or promises outside of the capacity of the insurance contract or trust fund to meet, he and the other creditors should be beyond any further pension claims. The employer should observe great care on this point—see the *New York City Omnibus* case—and should not guarantee the pensions nor firmly assert the absolutism of vesting.

Mr. Peterson's glance at the Government shadow as he closes his discussion reminds us to avoid creating difficulties and shortcomings in pension plans which might tend to lengthen this shade.

I am glad Dr. Stanley touched further on the problems of a trust fund when it is continued after the Plan itself has terminated. Perhaps, however, if the coverage under the terminated Plan is quite sizable, no immediate rush to translate the assets into fixed annuities is necessary. It might be an awkward time to liquidate the investments. For the time being the fund could meet the pensions as they fall due and take time to organize itself—with respect to allocations, choice of insurance company, treatment of disability pensioners, closing-out expenses, etc.—and in due time effect the annuity purchases. Most trust-fund plans do not require annuity purchase, but make it permissive.

Dr. Stanley observes that in termination cases with which he is familiar and which involve my Exhibit 8 type of clause no difficulty has been experienced, and that a practical construction has been put upon what I consider vague language such that definite pensions can be effected without the hiatus of doubt that I mention in the paper. Probably this construction was taken by the union, or by union-management agreement, without individual employee signatures or waivers. This experience to date does not change my feeling that the clause could be challenged on the grounds of literally saying something quite different. To take an extreme example for the age 60–64 category, if, at termination of plan, I were an employee age 60 with an accrued pension of $60 a month and there were only one other employee in this category, he being age 64 with $60 also, and if we had to share a fund such that after a one-year deferred annuity purchase for him of $25 a month there was enough to provide me with

$25 on a 5-year deferred annuity basis, then if he should die before 65 I would still get only my $25. The whole fund, on the other hand, with him gone before age 65, would have given me my full $60. In such a situation, I should be inclined to challenge the interpretation and ask for my $60 pension.

In Mr. Fellers' comments he, also, cites certain cases which either have by-passed the termination language or have made esoteric interpretations thereof. Now, this can probably be done in many cases, but sometimes the Plan is going to be expected to deliver what it says and I am not complacent about effecting transactions not in conformity with the language. If interpretations can change one part of a Plan from what is written, how "good" are the other provisions? Here is something perhaps more dangerous than Mr. Peterson's "fine print."

The only recent cases which have gone to court, as far as I know, are the N.Y. Omnibus matter, turning on alleged commitments of the employer (and the employer's interpretation lost out), and the Kaiser-Frazer Motor Company termination of Plan. Rather supporting my views above, this latter has just been upheld in its second court trial to the effect that no *ad hoc* arrangement or agreement to divide up the fund in cash among all prior participants will be permitted but rather that the termination clause of the Plan shall govern and provide the original product intended, *viz.*, age and disability pensions. The Court[1] found that it "may not rewrite the contracts here involved" and stated in summary:

> Termination of operations at employer's principal plant and its curtailment of operations at other plants held not to warrant termination of pension trust for retired employees and distribution of trust fund between retired employees and remaining employees, such termination of the trust and distribution of the fund being inconsistent with the plan and purpose of employer and union as set forth in agreements establishing the trust.

I am glad Mr. Fellers has brought out some illustrative figures showing relationships between reserve liabilities (I prefer this term to his "accrued liabilities") according to different actuarial contribution structures. However, since the single premium type is the only one not dependent on an assumption of the size and incidence of future contributions—which contributions, obviously, will not be forthcoming—I adhere to my general preference for the single premium method of measurement whenever the benefit is susceptible of being expressed on an "accrued to date" basis.

[1] Michigan Supreme Court, *George et al. v. Haber et al., as Trustees of Kaiser-Frazer UAW-CIO Retirement Fund*, October 3, 1955.

Mr. Attwood, from his practical experience in the military contracting field, gives us concrete examples of the "mass termination" problem and the interplay of nonvesting and "actuarial error." If the fund is mostly used up by vesting benefits in the mass terminations—in contemplation of death (of Plan) as it were—then the small or nonexistent residual minimizes the subsequent reversion to the contractor or, if passed on, to the Government. If, on the other hand, the mass terminations are not vested by the terms of the Plan or by an agreed-upon interpretation thereof, a large "actuarial-error" residual should not be divided up among only a handful of remaining employees; to do so would be a melon-cutting windfall of inordinate proportions. However, I should think a pension plan situation wherein exists a probability that excess funds would develop could still contain and "live with" a definite termination-of-plan clause if it is provided in the plan that the employer (or, if passed on, the Government) would be entitled to any amounts in excess of the sums needed to provide the remaining employees with their accrued pension interests. I wonder if the litigated cases Mr. Attwood mentions may not be under plans which omitted this provision?

Only as a footnote in that part of my paper discussing the termination-of-plan provisions in group annuities did I touch on unmaking and reapplying past service purchases once they had been made. I mention that a few contracts I had seen admitted of this action in event of the plan's termination. Furthermore, in any contract containing a temporary limitation clause of the sort required by the Internal Revenue Service (Mimeograph 5717), this action might be required upon termination of plan within its first ten years.

It is, therefore, of interest to hear from Mr. Rudd on this point. In Canada, as he points out, they do not have a governmental regulation like our Mimeograph 5717, and I infer that his contract form, likewise, was silent as to any reallocation from purchases already made. By unilateral action, therefore, in one type of case he cites, those already favored by the *fait accompli* of actual past service purchases agreed to divest themselves in favor of junior employees—a generous act. In his other example, however, I infer that the person whose nest was already feathered intended to hold on to what he had.

I am sure that Mr. Williamson, were he dining on oysters with the Walrus and the Carpenter, could turn their lucubrations on "cabbages and kings" into a relevant discourse on Social Security. His remarks on my paper do turn, quite appositely, the priority categories and single premium value concepts which I set forth, onto the scene of federal old-age and survivors insurance. He finds the reserve liability unmet, even for the first category of present beneficiaries. He could have found a similar situation in two other federal pension programs, the railroad retirement system and the civil-service retirement fund. Because of the taxing power or alleged federal guarantees, some students condone this situation in all three of these systems, while some condone it only in respect of the OASI, claiming that the other two should maintain a higher funded level, being more in the nature of staff pension plans, with employee contributions to account for and to refund in one way or another.

The topic of this paper was a rather difficult one to grapple with, surrounded with a penumbra within which play many vague and untested elements of an actuarial, legal, accounting and statutory nature. I wish to thank all those who, by their discussions, have helped expand the subject.