TRANSACTIONS OF SOCIETY OF ACTUARIES
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DIGEST OF INFORMAL DISCUSSION

RETIREMENT PLANS FOR SELF-EMPLOYED

A. Has the encouragement given to these plans through tax relief resulted in their more widespread use in Canada and Great Britain? What special policies have been developed to take advantage of the sales opportunities created by this type of legislation? What problems and difficulties have been encountered due to the form of the legislation? What methods have been developed to take care of the varying amounts of premium exemption year by year due to varying incomes?

B. What is the outlook for similar legislation in the United States? What changes in plans and contracts now being issued would be appropriate to take advantage of the benefits of such proposed legislation? Would it significantly change the current tendency of reducing the definition of the minimum size of group annuity or pension to secure tax advantages not now available on an individual policy basis? How may existing individual or group programs be adapted? What should be the basis for the determination of the deductible savings premium in a policy which provides both insurance and savings?

LEGISLATION IN GREAT BRITAIN AND CANADA AND PROPOSED LEGISLATION IN THE UNITED STATES

Great Britain, in 1956, and Canada, in 1957, passed legislation permitting premiums and deposits on individual retirement savings plans to be deducted up to certain limits from current income in making income tax returns. A bill with the same object has been introduced in the United States Congress. The following notes give the essential features of the legislation and, so far as available, the methods of administration.

GREAT BRITAIN

1. *Introduction*

Sections 22 to 26 of the Finance Act 1956 of the United Kingdom enacted in August 1956 authorized certain income tax allowances in respect of premiums paid on annuity policies of a prescribed form contracted by individuals who derived their earned income from other than pensionable employment. Such policies had to have for their main purpose the prôvision of a retirement pension for the applicant. As a consequence of such relief being granted the Act provided that any resulting annuity payments should be taxed as earned income to the extent that such payments arose from premiums on which relief was granted.

Broadly the individuals who are eligible to take advantage of these provisions are those who earn income from an office or employment, other than an office or

employment under which pensions are provided by a sponsored superannuation scheme, that is, a scheme to which the employer contributes. The annuity may be provided either by a contract made between the individual and a person lawfully carrying on in the United Kingdom the business of granting annuities on human life, or under irrevocable trusts established and administered in the United Kingdom for the benefit of individuals engaged in a particular occupation. In both cases the contracts under which the annuities are provided require the approval of the Inland Revenue.

The interest income earned by an insurance company or a trust in respect of this type of business is exempted from income tax.

2. *Income Tax Exemption*

Income tax relief is granted by allowing the premium paid under such a contract as a deduction from earnings in the year of assessment in which the premium is paid. The maximum amount so allowable in any one year is the lesser of £750 or one-tenth of net relevant earnings. Net relevant earnings means earned income for taxation purposes less income received from pensionable employment and certain other special deductions.

For persons aged over 40 at the date of enactment it was recognized that an annual premium of £750 would not necessarily provide an adequate pension. For this reason the maximum allowance was increased for persons born in 1915 or earlier except for those persons already in receipt of a pension under a sponsored superannuation scheme or having acquired rights to such a pension in future.

If in any year earnings are insufficient to claim the full amount of the premium the deficiency may be carried forward and treated as the amount of a qualifying premium paid in the next following year, and so on for succeeding years if necessary.

3. *Policy Provisions*

The Act requires that the Inland Revenue can only approve a contract provided it does not

a) provide for payment during the life of the policyholder of any sums except sums payable as an annuity for life; such annuity may however be guaranteed for a period of not more than ten years.

b) provide for the annuity to the policyholder to start before attaining age sixty or after attaining age seventy. Exceptions may be made when the policyholder's occupation is one for which retirement is customary before age sixty (in which case the minimum permitted age is fifty) or on disability retirement.

c) provide for payment by the company of any other sums, except an annuity payable to a deceased policyholder's spouse or approved dependent, or, if no annuity becomes payable under the contract, a benefit equal to return of premiums with a reasonable rate of interest and any attaching bonuses.

d) provide an annuity to a deceased policyholder's spouse or dependent for an amount greater than that to which the policyholder was entitled.

In addition the Act requires that the policy must contain a provision to the effect that no annuity payable under it shall be capable in whole or in part of surrender, commutation or assignment.

As a consequence of the provisions of the Act the policy must contain a stipulation that if the policyholder ceases to be eligible for relief, or if the Inland Revenue withdraws its approval, the company will refuse to accept further premiums.

4. *Income Tax on Payments under the Contract*

Any annuity payments are treated as earned income to the extent they are derived from premiums on which relief has been granted.

Lump sum payments can only be made by way of death benefit. Such death benefits, or the value of annuities to the surviving spouse or dependent will be liable to estate duty.

5. *Duties of Issuing Company*

The issuing company must satisfy itself that the applicant is one who is eligible for relief under the Act. This requires completion by the applicant of a special statement, designed so that the company may be in a position to determine whether he is eligible or otherwise. Doubtful cases are referred to the Inland Revenue.

Once a contract is issued the company is required to make periodical inquiries, the first not more than 30 months after issue and thereafter at intervals of not more than 3 years, to ensure that the policyholder continues to be eligible. If he ceases to be eligible then no further premiums may be accepted and the contract continues as a paid-up contract. The company must also issue an annual reminder to the policyholder that premiums should cease if he is no longer a qualifying individual.

The company cannot enter into a contract, or series of contracts, for a premium of over £750 per annum or such higher maximum amount as may be allowable for persons born in 1915 or earlier. It is not, however, expected to ascertain to what extent the proposed premium will qualify for relief to the individual.

6. *Procedure*

When an annuity is issued the office is required to provide the annuitant with a standard approved form which gives the essential particulars of the contract and includes a statement that the form of contract has been approved by the Inland Revenue. The issue of such a form does not, however, mean that the policyholder is necessarily entitled to relief; this is a matter which the Inland Revenue will decide. Its purpose is to provide evidence, which the policyholder can submit to the Inland Revenue, that he has effected such a policy.

7. *General*

The insurance companies operating in Great Britain offer a large variety of plans conforming with the requirements of the Act. The main differences are in

the death benefit prior to retirement, which may consist of return of premiums with or without interest or a reversionary annuity to the annuitant's spouse. In some policies there is no death benefit. In most instances the policy is nonparticipating, but a few companies issue a plan on the participating basis. Some companies have recognized that a level premium plan is not ideal when the policyholder's income may be subject to wide fluctuation and offer alternative plans based on single premiums.

CANADA

1. *Introduction*

Section 79B of the Income Tax Act, enacted at the 1957 session of the Parliament of Canada, and assented to on April 12, 1957, authorizes income tax exemptions for deposits made on a Registered Retirement Savings Plan and provides for income tax assessments on payments out of such a plan.

A Registered Retirement Savings Plan must be a contractual arrangement between a taxpayer and an authorized corporation under which, in return for the deposits made by the taxpayer, the corporation agrees to provide him with an income for life, commencing not later than age 71, with the provision that no payment may be made to the taxpayer before the income commences, but that on his prior death the deposits made may be refunded with interest to a specified beneficiary.

An authorized corporation may be a corporation licensed to sell annuities (which in Canada means a life insurance company or a Government Annuities office), a trust company, or a corporation licensed to issue investment contracts providing for the payment of a determinable amount at maturity. In the latter two cases the accumulated funds under a contract must be used to purchase an annuity for life from a corporation licensed to sell annuities.

The following sections are applicable primarily to Registered Retirement Savings contracts issued by life insurance companies, but the same general principles would be effective in the case of plans set up by other corporations.

2. *Income Tax Exemptions*

The taxpayer who has set up a retirement savings plan under which he is to receive the retirement income may claim income tax exemptions on his deposits as follows:

An employee who is a member of a Registered Pension Plan through his employer may supplement the tax exempt contributions which he may be making through his employer's plan with further tax exempt retirement savings as an individual, but the total of such contributions and retirement savings claimed for income tax exemption must not exceed $1,500 or 10% of his earned income, whichever is less.

For a person who is not a member of a Registered Pension Plan through his place of employment, the amount claimed must not exceed $2,500 or 10% of his earned income, whichever is less.

Claims for exemption in respect to any taxation year may be made for "any

premium paid by the taxpayer under the plan during the taxation year or within sixty days after the end of the taxation year (to the extent that it was not deductible in computing his income for a previous taxation year) not exceeding, however," the amounts stated in the preceding paragraphs.

There is no other provision for carrying forward excess contributions or unused exemptions to a subsequent year; nor is there a provision exempting from taxation that part of payments out under the plan which may arise from premiums for which exemption could not be claimed.

3. *Required Policy Provisions*

All life insurance policies which include a savings element are eligible for registration, but only the savings portion of the premiums will qualify for tax exemptions. The determination of the savings portion is described in Section 7.

To be eligible for registration the policy must contain the following provisions, either as part of the contract itself, or as an amendment to the contract applied for and agreed to by the policyholder:

(1) The policy may not be assigned.

(2) The cash loan privilege, automatic premium loan privilege, and extended term insurance privilege must be eliminated, and in the event of default in premiums it must be provided that the policy will be automatically changed to a reduced paid-up policy under the paid-up policy privilege.

(3) The cash value privilege may be exercised only for the purpose of obtaining a life income as described in (5) below.

(4) The right to receive a lump sum settlement at retirement must be eliminated.

(5) The policy must contain a provision that it will be terminated before the age of 71, and that at termination the value of the policy will be applied to provide an annuity under the following conditions:

a) The annuity is to be payable during the lifetime of the policyholder or during the joint lifetime of the policyholder and his spouse and the lifetime of the survivor.

b) The guaranteed period under the annuity may not exceed 15 years unless the policy was issued before March 14, 1957, in which case the maximum period may be 20 years.

c) The annuity is to provide equal payments to the policyholder throughout his lifetime, except that dividend payments may be made by the company, and also that the annuity may be adjusted so as to provide a higher income before 70 than thereafter, the difference being not greater than the pension which it is expected will be received commencing at age 70 under the Old Age Security Act. Payments after the policyholder's death for the remainder of a guaranteed period or to his spouse under a Joint and Survivor Annuity must also be equal to one another and may be lower than the original level, but the income of the policyholder after the death of his spouse may not be reduced.

d) The annuity must not be capable, in whole or in part, of surrender, commutation, or assignment. (This has been defined to mean, in part, that in-

come payments during the remainder of the guaranteed period following the policyholder's death may not be commuted.)

(6) If the policy provides for participation in dividends, all dividends allotted before retirement must be left with the company and used to increase the annuity at retirement.

(7) No provision giving the policyholder a contract right to cancel the above provisions may be included in the policy. (It is permissible to say in letters, literature and advertising that cancellation of the above provisions is contemplated by the legislation, but no statement may be made in such letters, literature or advertising which implies that the financial institution administering a registered retirement savings plan is agreeing in advance that it will accept at some future date chosen by the annuitant an application for cancellation. Any such statement may result in a ruling by the department of National Revenue that contracts affected by the statement are not acceptable for registration.)

4. *Income Taxation on Benefits Payable on Death before Retirement*

In the event of the death before retirement of the holder of a Registered Retirement Savings Plan, that part of the payment out which is considered to represent the savings accumulated up to the date of death is taxable as income to the recipient at a fixed rate of 15%, no matter what the total income of the recipient in the year may be.

The part of the death benefit payable which is to be considered as accumulated savings and thus taxable, is to be the greater of (*a*) the cash surrender value of the policy at the date of death together with any dividends then at credit, or (*b*) the sum of the savings premiums paid calculated on an annual premium basis.

The death benefit may be paid in instalments under the settlement options, in which case the income tax liability will be spread over the period of instalment payments.

5. *Income Taxation on Retirement Income*

The annuity payments after retirement under a Registered Retirement Savings Plan are to be included in the taxable income of the annuitant in the taxation year in which they are received.

6. *Income Taxation after "De-registration"*

As mentioned in Section 3, the law contemplates the possibility that the holder of a Registered Retirement Savings Plan may apply to the company to have the special provisions of his policy canceled so that it is thereafter ineligible for registration. After such "de-registration" any payment made by the company which can be considered as a payment of accumulated savings, including the payment of death benefits, is to be taxable as follows: The company is required to withhold 25% of each such payment made and remit this sum to the Receiver General of Canada on account of the income tax of the payee. The payee is required to include the whole payment, including the amount withheld, in his taxable income for the year. If the 25% withheld is less than the additional

tax assessed in respect of the payment, the extra amount is payable by the taxpayer. If, on the other hand, the 25% withheld is more than the extra tax assessed, the excess is not refunded but is, in effect, charged as a penalty.

Payment may be made in instalments, in which case the tax would be assessed year by year on the amount paid during the year.

7. *Determination of Savings Premiums*

In the case of plans of insurance providing only (*a*) an annuity at maturity, and (*b*) a benefit at death before maturity not exceeding the return of premiums with interest and dividends, the whole premium payable will qualify as a savings premium.

The savings portion of the premium on other plans will be determined by deducting from the total premium

(1) premiums charged for disability, accidental death, family income, term insurance riders, and other additional benefits,

(2) premiums charged for any additional mortality risk under the policy,

(3) a nonparticipating gross level term insurance premium payable to the policy anniversary nearest age 65 or to the prior maturity of the policy calculated on the basis of standard mortality as being sufficient to cover the excess of the death benefit provided by the policy contract over the savings fund being accumulated. The net level term insurance premium is the difference between

a) the net level premium required to provide the total death benefit payable under the policy before age 65 or the maturity date, if earlier, and the surrender or maturity value at age 65 or the maturity date, the calculation being made on the A1924–29 ultimate mortality table with $3\frac{1}{2}$% interest, and

b) the net level $3\frac{1}{2}$% sinking fund premium required to accumulate the surrender or maturity value.

To obtain the gross term premium the net premium is loaded 15% of itself and $1.25 per $1,000 of face amount.

The remainder of the premium after making the three deductions as required is considered to be the savings premium eligible to be claimed for income tax exemption.

8. *Registration of Existing Policies*

Existing policies which are free of indebtedness and not assigned are eligible for registration as retirement savings plans on the following basis:

(1) The insurance and savings elements of the premium will be calculated as if the policy had been registered from the date of issue.

(2) The existing savings element built up at the date of registration will be determined and this amount, with subsequent interest earnings, will be free from income tax under Section 79B on payment out.

The device adopted for segregating nonregistered savings is to determine the paid-up value which could have been granted under the policy at the date of registration and place this paid-up value on record. At any subsequent transaction the then cash value of this paid-up policy would be considered as nonregistered savings, not subject to tax under Section 79B. Similarly, if there are

accumulated dividends or bonuses attached to the policy at registration, they may be segregated and made free of tax, as regards both the cash value at registration and subsequent increases due to interest earnings. The part of the retirement income arising from nonregistered savings would be taxable on its interest element only in the normal way.

Although savings accumulated to the date of registration would be free of tax when paid out, it is possible they may still have to be "locked in" in the same way as registered savings owing to the great complications which would arise if payments out are permitted.

In the case of an existing policy which is registered, the taxation provisions which are described in Sections 4, 5, and 6 will, therefore, apply only to the part of any payment out under the contract which arises from premiums paid after registration.

As the law now reads, the registration of existing policies with protection for existing savings from taxation is applicable to policies issued before the end of 1957. It is believed, however, that amendments may be made which will permit the late registration of policies issued in subsequent years.

9. *Methods of Registration*

In addition to the agreement of the policyholder, and in some cases his beneficiary, to the alterations in his policy which are required to make it eligible for registration, the company must obtain from the policyholder a direct request that his contract be registered and an acknowledgment that he understands that payments to him or to his beneficiary will be subject to tax under the provisions of the Income Tax Act (Canada).

In order to register retirement savings plans the company is to send to the Department of National Revenue periodically, or at the end of the calendar year as it chooses, a list in duplicate of the numbers of the policies which its policyholders have requested should be registered. One copy of the list will be returned to the company with an indication that the contracts have been registered and this will be authority to the company to issue to the policyholder a special form of premium receipt or certificate setting forth the amount of the savings premium which he has paid, which receipt or certificate is to be filed by him with his income tax return.

The company is required to keep on record the duplicate list returned by the Department of National Revenue so that if at a later date it becomes necessary for the authorities to establish that a contract was registered, they can look to the company's records for assistance.

Registration of a contract at any time during a taxation year confers on the policyholder the right to claim tax exemption in respect to any premiums paid during the taxation year, even though paid before the date of registration. In normal cases the effective date of registration will be the date the request for registration is received by the company from the policyholder and not necessarily the date of the return of the lists from the Department of National Revenue.

10. *General Comments*

The regulations of the Department of National Revenue under Section 79B of the Income Tax Act are not yet in their final form. The problem has been to develop a workable system on the basis of the legislation now in force. Some modifications might be possible if amendments to the law are made.

UNITED STATES

1. *Introduction*

Legislation to facilitate the development of pension plans for self-employed persons is now pending in Congress in the form of the so-called Jenkins-Keogh Bill. So far at this session, it has made no progress.

The stated purpose of the legislation is "to encourage the establishment of voluntary pension plans by self-employed individuals." This would be accomplished by making their contributions to pension retirement programs currently deductible from gross income and postponing the tax until distribution or following age 65.

Amounts to be deducted would be known as "retirement deposits." They could be qualified either by paying money into a so-called "restricted retirement fund" administered by a bank under a trust or a custodian agreement or by paying premiums to a life insurance company under a "restricted retirement policy." This would include either an existing or new "annuity, endowment or life insurance contract, or combination thereof, other than a term insurance contract." The legislation also contemplates that the trustee or custodian of a restricted retirement fund may invest in such a policy on the life of an individual contributor to the fund, in which case the individual would receive the same tax treatment as though he invested directly in the contract.

In what follows, comments apply primarily to the use of the restricted retirement policy and the life insurance company.

2. *Income Tax Exemptions*

There would be deducted from gross income that part of the premium which is not allocable to the life insurance protection, to be determined under regulations prescribed by the Secretary of the Treasury. Presumably, the same rules for separating the premium would be followed as are now employed in the case of employee pension plans.

The maximum annual deduction permitted would be 10% of net earnings from self-employment or $5,000, whichever is the lesser, with an over-all lifetime limit of $100,000. Special provision, however, would be made for increased annual deductions in the case of those individuals who are over age 50 at the time the bill is passed and for carry-over of unused deductions from one year to another.

3. *Required Policy Provisions*

In earlier versions of this legislation, the use of policies with restricted withdrawal privileges was considered. This arrangement was discarded, since such

restricted policies appeared to be in conflict with standard provision and standard nonforfeiture statutes in the states. Instead, it was decided to use the standard type policies which permit withdrawal, but to provide for the imposition of a tax penalty if and when withdrawal should actually take place. The contracts to be used, therefore, would be the usual type of insurance and annuity contracts. When used as a restricted retirement policy, the policy would have to be endorsed with the words "restricted retirement policy pursuant to Section 217 of the Internal Revenue Code." This would not conflict with existing statutes.

4. *Income Taxation on Benefits Payable on Death before Retirement*

Amounts paid to a beneficiary or the estate of the insured under a restricted retirement policy, by reason of the insured's death, would be includible in the gross income of the beneficiary in the year in which paid, to the extent that they were attributable to premiums deducted by the insured. Paralleling the treatment accorded life insurance under employee pension plans, this would contemplate that the proceeds, to the extent of the reserves on the contract, would be included as income inasmuch as the "net amount at risk" is presumed to be paid for by the part of the premium not deductible by the insured.

5. *Income Taxation on Retirement Income*

Amounts paid to the insured after retirement under restricted retirement policies would be taxed as annuity income under Section 72 of the Internal Revenue Code.

6. *Income Taxation on Lump Sum Payments*

In the event that the entire interest of the insured under all of his restricted retirement policies is paid to him after age 65 and after his policies had been in force for at least 5 years, or is paid to his estate or his beneficiaries after his death, the tax would be limited to an amount not exceeding five times the increase in tax which would result from the inclusion in the recipient's gross income of 20% of the amount distributed to him. This, of course, would have the advantage of measuring the tax by lower tax bracket rates.

The legislation would permit withdrawal of equities under restricted retirement policies prior to age 65, subject to a tax penalty designed to discourage such withdrawal except where necessary to meet pressing economic needs. If the insured should withdraw all or part of his investment in a restricted retirement policy prior to age 65, he would be required to pay a tax equal to 110% of the aggregate amount of taxes he would have paid had he received the withdrawal in equal instalments in his current taxable year and the four taxable years immediately preceding.

Borrowing against the policy (except temporary borrowing to pay premiums) would be deemed to be a taxable payment to the insured to the extent of the loan. Likewise, if a nonforfeiture option becomes operative under the policy (except reduced paid-up insurance), an amount equal to the cash surrender value would be deemed to have been paid to the insured.

7. *Determination of Savings Premiums*

The part of the premium under a restricted retirement policy deductible as a retirement deposit would be determined under regulations to be prescribed by the Secretary of the Treasury. Presumably, these regulations would follow those applicable to employee pension plans. In such cases, it is assumed that an amount equal to the one-year term premium on the net amount at risk represents the insurance portion of the premium and the remainder represents the savings portion.

8. *Registration of Existing Policies*

Outstanding policies could be endorsed as restricted retirement policies. In the event of subsequent surrender of the contract or borrowing against it, the loan or nonforfeiture value, to the extent it had accrued prior to the registration of the contract, would be free of any restrictions.

9. *Methods of Registration*

The insured would notify the life insurance company that he intended to make payments on a specified policy or contract. Within 60 days thereafter, the insurance company would endorse the contract as a "restricted retirement policy pursuant to Section 217 of the Internal Revenue Code" and would file an information return with the Treasury. The policy or contract would also have to be made nonassignable. The insurance company would probably be requested by the insured to inform him what portion of each payment would be deductible.

If the policy or contract should subsequently be surrendered or borrowed against, or if a nonforfeiture option (other than reduced paid-up insurance) becomes operative, the company would be required to file a further information return. This return, however, would not be required in the case of the exercise of rights to any cash loan or nonforfeiture value to the extent it had accrued prior to the registration of the contract.

10. *General Comments*

Legislation of similar character has been before Congress since 1951 under the sponsorship of professional self-employed persons such as doctors, lawyers, actors, etc. The American Bar Association has taken a particular interest in sponsoring this legislation and recently has been instrumental in organizing "The American Thrift Assembly for Ten Million Self-Employed" to promote it. This legislation has encountered two main objections. First, the Treasury Department has been opposed to it on the ground that it would seriously cut into tax revenues. Second, while eliminating a present tax discrimination against the self-employed, it would open up a new discrimination between the self-employed and those employed who are not now covered under employee pension plans. The latter could not be covered under this legislation without still further cutting into tax revenues.

MR. J. A. CAMPBELL felt that the recent passage of tax relief legislation in Canada has led to widespread interest in retirement plans, but that

their actual use to date has not been extensive. He pointed out that life companies have been somewhat less active in promoting these plans than have trust companies. In general, the life companies have used their existing policy forms, supplementing them only by the introduction of contracts designed to extend the maximum tax advantages to those with varying incomes.

There are small difficulties, such as inability to commute remaining guaranteed payments in case of the death of the annuitant, but Mr. Campbell felt that methods may be devised for overcoming them. The chief difficulty, in his view, arises out of the penalties imposed if a policyholder wishes to withdraw from a registered plan, particularly if such plan is a life insurance plan and not an annuity. The only option available in case of premium default on a life plan is reduced paid-up insurance; thus, frequently at a time when insurance protection is most needed, such as during a severe illness, there may be a substantial reduction in coverage. Furthermore, the insured has no right to surrender a part of his policy for funds to cover emergency needs. Mr. Campbell noted that more flexibility would be achieved if a registered policy could be split into two parts, one of which would be eligible for surrender values. He pointed out, however, that this would result in administrative difficulties.

Companies must be cautious in recommending registration and should assure themselves that policyholders requesting it have a clear understanding of the modifications and limitations of their protection.

MR. T. B. MORRISON felt that, with the higher investment yields now prevailing, insurance companies are at some disadvantage as compared to other investment media which may be used for registered retirement savings plans in Canada. This situation arises because the insurance companies must calculate reserves at an interest rate not exceeding $3\frac{1}{2}\%$.

In promoting these plans, a life underwriter must recognize that the restrictions entailed in registration may impair a contract's usefulness in many situations; furthermore, a point to be considered is that the legislation does not provide a tax exemption, per se, but is rather a form of tax postponement which may or may not result in eventual tax savings.

Mr. Morrison described retirement annuities offered by his company which are specially designed for use as registered retirement savings plans. The income bases in these plans are more favorable to the purchaser than otherwise similar plans not designed for registration, because there is no cash option and the optional forms of income available are of limited scope. These plans include provisions allowing the purchase of single premium retirement annuity riders from time to time, at rates in effect at the time of purchase.

Although it is tempting to contemplate a group approach in making these plans available to members of professional organizations, Mr. Morrison's company believes that the problem is so individual in character as to vitiate any economies of operation resulting from so-called group handling.

MR. J. E. MORRISON, speaking on section A, described an annuity policy designed by his company for those wishing to realize the tax advantages of the new Canadian legislation. It is available only if registration is requested at issuance of the policy.

The new policy consists of two parts; one is a basic annual premium annuity without insurance, and the other is an additional deposit provision to permit flexibility in premium payments.

The basic coverage is a life annuity commencing at age 70 with a ten-year guarantee. The additional deposit provision permits the policyholder to purchase single premium paid-up annuities of the same form as the basic policy, at any time, as long as there has been no default in payment of the basic premiums. Each deposit must be at least $100, and total deposits in any one year may not exceed twice the basic premium. Single premium rates are guaranteed by contract for all policy years to maturity.

Various other provisions for flexibility have been included. The policyholder may elect an earlier commencement date after age 60; he may select other annuity forms; the usual settlement options are available to the beneficiary for amounts payable on death of the annuitant before his annuity payments commence.

The policy is nonparticipating during the first 5 years, and participating thereafter for both the basic and the additional deposit benefits. While the policy is registered, dividends are left with the company to accumulate.

The guaranteed return under this policy is improved over the Company's regular Annual Premium Retirement Annuity contract. Because of the "locked-in" features of this plan, a more liberal settlement option basis has been assumed, and lower expenses are anticipated under the additional deposit provision.

MR. J. G. FLETCHER, speaking on section A, pointed out that the Canadian Government is itself in the annuity business, selling both deferred and immediate annuities at net rates, with administration costs borne by the government. About 90% of its new sales are registered. Since government annuities have never had a surrender value, the "locked-in" requirement of the newer registered plans is not a deterrent to acceptance by clients already familiar with the older nonregistered plans.

Some problems are foreseen in connection with the maximum contribu-

tion eligible for income tax advantages. Records show that some people are making contributions in excess of 10% of earned income, and do not seem to realize that no tax credits are allowed on the excess, while income tax on the full annuity payments will ultimately be due. A solution would involve education of the buying public as to the extent of the tax advantages, and in those cases where the contributions exceed the limits for tax credits two contracts might be issued, only one of which would be registered.

Another problem arises out of the provision that any premium paid during the tax year or within 60 days after the end of the tax year and within the specified amount limits must generally be claimed for exemption in that tax year. As the law now stands the first contribution year will be 14 months to March 1958 and contribution years thereafter will run from March to March. This was not the original intent of the legislation and some modification is anticipated. Another expected amendment, and one which seems desirable, is a provision to permit commutation of the remainder of guaranteed payments in the event of the death of the policyholder.

MR. W. M. ANDERSON confined his remarks to a discussion of the 60-day rule under the Canadian legislation. As Mr. Fletcher had stated, it was evidently the original intent of the legislature to allow a 60-day period at the beginning of each tax year as an optional period where the taxpayer, having paid money into registered retirement plans, could claim it for the previous tax year or current tax year. However, as the law is worded, there is no option and contributions made within the 60-day period must be deducted in the previous year to the extent that they are eligible, and only that portion which is not eligible may be credited to the current tax year.

While it would be preferable to amend the law to conform to the original intent of the legislature, the retention of the 60-day provision, even as it now stands, is more desirable than its complete elimination or the adoption of a shorter period. This is especially true from the point of view of life insurance companies whose heavy work load in January and February would be overburdened by the necessity of certificate filing during this period.

MR. F. B. DANA limited his remarks to a discussion of the Canadian Medical Retirement Savings Plan which was developed as a result of the Canadian tax legislation.

Sponsored by the Canadian Medical Association, the plan uses group rather than individual policy methods and provides retirement annuities only, without insurance. The services of a bank, a trust company, and an

insurance company are used. Each participant remits his contributions to the participating bank, which transfers such contributions quarterly to the trust or insurance company in the proportions elected. Contributions to the trust are placed in a pooled fund which is invested in common stocks. On retirement, the share of the fund standing to the participant's credit is used to purchase an annuity from any insurer elected by the participant. In order to hedge against the possibility of depressed share values at the time of retirement, the participant may direct that withdrawals be made quarterly over a five year period preceding retirement.

Contributions made to the participating insurance company are accepted under a deposit administration group annuity contract. The rates at which annuities will be purchased at retirement are generally guaranteed, with a somewhat less favorable guarantee for sums transferred from the trust fund at retirement.

The plan is quite flexible, generally allowing contributions ranging upward from $300 per year. The basis of allocation between the trust company and the insurance company may be changed as often as once a year, but a minimum of $100 must be allocated to the insurer to obtain the guaranteed purchase rates.

No reliable figures are available as to extent of participation, but interest in the plan has been greatest among younger members and those living in rural areas.

MR. JOHN GORHAM said that the recent Canadian legislation has resulted in widespread interest by professional and other associations in the possibility of providing annuity benefits on a group basis. He pointed out that such plans might be attractive because of expense savings resulting from reduced commissions, lower collection costs and simplified administration. Lack of personal service by an insurance agent would largely offset reduced commissions; collection costs can in suitable cases be lower, but this is not automatically so even though collections are made by the association; and reduced administration costs will depend largely on the extent to which the association itself is prepared to participate in administering the plan.

This area of business is still experimental and the merit of group underwriting would vary with the nature of the association.

A particularly interesting example was the plan recently installed for the Canadian Medical Association, under which contributions are collected through approximately 700 branches of the Bank of Montreal, and under which the association handles a large part of administrative detail.

MR. J. M. MILLER confined his remarks to a difficulty encountered in the Canadian legislation, to the effect that the annuity must not be

capable, in whole or in part, of surrender, commutation or assignment. This has been interpreted to mean, in part, that income payments during the remainder of the guaranteed period following the policyholder's death may not be commuted. This interpretation, when applied in the case of remaining guaranteed payments which become payable to an administrator or executor of the payee's estate, seems contrary to the intent of the law which specifically permits the annuity "in event of the death of any person to whom such annuity is payable, to be assignable by the heirs, executors, administrators or other legal representatives of such person in the distribution of his estate. . . ." The argument is that if a sum is "assignable," it may be assigned to an insurance company, or in the ordinary parlance of insurance, "commuted" for its cash value.

To unduly delay the final settlement of an estate by compelling companies to continue instalment payments over a period of years will result in unnecessary expenses and other hardships. It is doubtful that the law was designed to bring about such a situation, and it is hoped that new regulations or modifications of the law will soon be adopted to correct the situation.

MR. LACHLAN CAMPBELL pointed out that the British Finance Act 1956 restricts the form of "self-employed" contract which is eligible for tax advantages. Generally speaking, it is a deferred annuity with annuity payments commencing between age 60 and age 70. The death benefit, if any, is limited to return of premiums with or without interest or a reversionary annuity to a dependent, and no commutation is permitted.

Mr. Campbell then described a form designed by his Company within the limits of the Act. An interesting feature is that, in order to reduce the possibility of antiselection, an optional type of annuity must be elected at least 3 years prior to the first annuity payment.

The volume of business issued in Great Britain on "self-employed" contracts has not come up to expectations, partly because no commutation is permissible and partly because in Great Britain a portion of premiums paid for ordinary life and endowment policies is allowed as a deduction from income for tax purposes. This partial tax relief on premiums paid for endowments, plus the full relief on the capital element under annuities purchased with endowment proceeds, make a retirement program based on endowments as favorable in many respects as a "self-employed" deferred annuity which generally permits full relief on premiums, but the annuity payments are fully taxable as income.

British companies have generally used the British $a(55)$ annuity table as the mortality basis for the new plans. While this table is considered suitable for immediate annuities commencing in 1955, margins in other

factors would seem to be necessary to offset any future unfavorable experience which might develop as a result of further reductions in annuitant mortality.

MR. G. W. PINGSTONE, after pointing out that the income tax relief in the legislation in Great Britain is really relief for both income and surtax, noted that the types of policies which have been introduced in Great Britain have necessarily been limited by the restrictions imposed by the legislation, but within these restrictions a considerable degree of flexibility has been achieved. For instance, the majority of companies do not require immediate selection of the age at which the pension is to commence, policies are available with or without participation in profits, return of premiums may be with or without interest, and annuities to surviving widows may be provided whether death occurs before or after retirement. Arrangements which involve considerable departure from normal life assurance practice have also been devised. Among these are the use of a form of variable annuity and the use of a rate of interest geared to the company's own earnings or to the yield on a specified government security. Several approaches have been taken to answer the problem of varying premiums, and a number of companies issue annual premium policies with provision for premium variation within a specified period of time.

The introduction of these new contract forms has given rise to many problems. One of the most important is that of advising the "self-employed" of different types and at different income levels on the desirability of these plans. Mr. Pingstone felt that at the lower income levels the advantage in terms of net pension for a given net outlay is limited, and that the alternative of effecting an endowment assurance and using its proceeds to purchase an annuity should be carefully considered.

MR. K. A. USHERWOOD, judging from the experience of two British industrial-ordinary companies, his own and another, remarked that there has been considerable interest in retirement annuity contracts since passage of the British Finance Act 1956. In these companies such business has been transacted chiefly with the small businessman rather than the professional classes. However, the current rate of sales is undoubtedly high because of the backlog created prior to enactment of the legislation.

MR. H. A. R. BARNETT noted that the description of legislation in Great Britain and Canada and proposed legislation in the United States, which appears before the discussion of this topic, omitted one important, though temporary, feature of the Plan in the United Kingdom authorized by the Finance Act 1956. This feature provides that an individual may claim part of the premiums paid in the fiscal year ending April 5, 1958 as

an allowance against earnings for the fiscal year ended April 5, 1957. The provision was undoubtedly due to the inevitable time lag between introduction of the Finance Bill and the time the Plan would effectively be in operation.

Because of this, the question of more widespread use of retirement plans as a result of tax relief cannot be determined until after April 5, 1958, when it will no longer be possible to take advantage of the "time-lag concession."

MR. S. J. KINGSTON, speaking on section B, stated that the experience of his company in designing pension plans for groups of highly paid self-employed persons indicates that the following features are necessary:

1. Availability of a multiplicity of settlement options, and a flexible maturity date.
2. A death benefit before retirement equal to the reserve or some similar standard. Also, individual allocation of dividends is desirable.
3. Absence of life insurance protection (other than the reserve or like standard).
4. Ability to change premium from time to time as financial progress is made.
5. Ability to add outside investment funds at retirement.
6. A low minimum number of lives required to qualify, because such plans develop slowly at first, but rapidly after the plan is in effect.
7. Restrictions and penalties on early withdrawal.
8. A method of centralized billing.
9. Demand for high caliber of service and advice to individuals in the program.
10. Ability to carry on the program on leaving the group due to resignation or transfer.

Mr. Kingston's company has an individual annuity contract adaptable to these 10 requirements.

MR. G. N. WATSON expected that there will be a great deal of emphasis on issuing retirement savings plans on a group basis. While group handling in the case of professional associations may not be regarded as entirely satisfactory, life insurance companies which attempt to limit their operations in this field to individual policies only may find that large segments of business such as doctors, lawyers, etc., will be lost to trust companies and other organizations offering plans that would qualify for tax advantages. This is exemplified by the Canadian Medical Association plan, which might be a forerunner of other plans instituted by other professional associations.

It is highly probable that the rate of participation in a professional group which must be enrolled on the basis of a mail canvass only will not exceed 10% to 15% of the eligible members. Consequently, individual

solicitation by the ordinary agent will be the only means of effectively reaching the remainder through the sale of individual policies.

Mr. Watson felt that the trade association field might have certain advantages over the professional association field and that perhaps group pension policies have a more important application here than in the case of professional associations.

MR. B. E. SHEPHERD discussed the chances of legislation passing in the United States. He pointed out that an important feature of the United States plan as opposed to those of Great Britain and Canada is that there would be no "freezing-in" of proceeds, but amounts payable on surrender would be subject to tax penalties to control misuse.

Several professional groups, primarily the American Bar Association, are campaigning to get this proposed legislation enacted. A poll conducted among the members of the House of Representatives, which must be the originating body, generally indicates a very favorable reaction, but there is considerable opposition in the important Ways and Means Committee. In addition, the Treasury Department feels that such legislation will produce a drain on tax revenues. Finally, since the bill would be directed only to the self-employed, there is some feeling that it would discriminate against an estimated 40 million employed people who are not now covered under employee pension plans, and who would not be covered under the proposed plan.

MR. R. J. MYERS, speaking on section B, said that in the United States there has been a widespread feeling that self-employed persons should be covered under the Old-Age and Survivors Insurance program before receiving tax advantages of private pension plans. This constituted a barrier to legislation of the type proposed in the Jenkins-Keogh bill, until the passage of the 1956 amendments to the Social Security Act which extended Social Security benefits to all self-employed persons except doctors of medicine. Since social insurance legislation and tax legislation both originate in the House Ways and Means Committee, there is a close relationship between the two, and there is a possibility that the Jenkins-Keogh legislation may also be made applicable to all self-employed persons except doctors.