EBRI ISSUE BRIEF

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WOMEN AND PENSIONS
PART II: IMPLICATIONS OF PROPOSALS FOR REFORM

The Congress is currently considering legislation intended to increase pension receipt among women. To assist in evaluating such legislation, this issue brief provides information on the prospects for greater pension receipt among women under the pending proposals. EBRI's June 1983 Issue Brief discussed the maturing pension system, ongoing changes in women's work force participation, and the potential effects of these developments on women's pensions.

Would a Reduction in Plan Participation Age Increase Benefit Receipt?

The proposals to reduce pension participation age requirements from twenty-five to twenty-one raise important questions: (1) Would such changes affect a significant segment of the work force? (2) Would the number of retirees receiving pension benefits increase?

As shown in table 1, in May 1979, there were 11.1 million workers, ages twenty-one to twenty-four, in the United States. Of these, 5.1 million, or 46.4 percent were not covered by pension plans; i.e., they worked for employers who did not sponsor pension plans. An additional 2.6 million, 23.4 percent, participated in plans but were not vested. Slightly more than 1.1 million, or 10.3 percent, were vested in their current employers' plans. As shown in table 1, the remaining 2.2 million workers, 19.9 percent, worked for employers with pension plans but were not yet plan participants. Some of the workers in this latter group could benefit from adjustments that lower the participation age.

Of the 2.2 million covered workers who were nonparticipants, 54.5 percent were women. In 1979, there were slightly more than 39 million working women in the United States. Assuming that the 1.2 million women who were nonparticipants did not participate in plans because they were younger than age twenty-five, a reduction in plan participation age requirements to twenty-one "could" have produced up to a 3 percent increase in the 1979 female plan participation rate.

Table 2 shows, however, that of the 2.2 million covered workers who were nonparticipants: (1) 48.5 percent had been in their jobs less than one year; and (2) 13.6 percent worked less than 1,000 hours annually. Table 2 also shows that among women who were ages twenty-one to twenty-four: (1) 46.7 percent had been in their jobs less than one year; and (2) 14.6 percent worked less than 1,000 hours annually.

TABLE 1

Pension Status of Workers Ages 21 to 24 in 1979 by Sex

	Men (millions)		Women (millions)		Total Men and Women (millions)	
Noncovered	2.9	48.0% 1/	2.2	44.5% 1/	5.1	46.4% 1/
Participants						
not vested	1.5	25.2	1.1	21.3	2.6	23.4
vested	0.6	10.4	0.5	10.1	1.1	10.3
Nonparticipants	1.0	16.4	1.2	24.2	2.2	19.9
Total 1/	6.0	100.0%	5.0	100.0%	11.1	100.0%

Source: EBRI tabulations of the May 1979 Current Population Survey.

1/ Totals and percents may not sum exactly due to rounding.

TABLE 2

Male and Female Workers Ages 21 to 24 in 1979 Who Did Not Participate in Their Employers' Pension Plans Due to Short Tenure and Part-Time Work

	Men (millions)		Women (millions)		Total Men and Women (millions)	
Less than one year in current job	0.5	50.6% 1/	0.6	46.7% 1/	1.1	48.5% 1/
One year or more in current job	0.5	50.4	0.6	53.3	1.1	51.5
Total covered nonparticipants 1/	1.0	100.0%	1.2	100.0%	2.2	100.0%
Working less than 1,000 hours annually	0.1	12.4	0.2	14.6	0.3	13.6

Source: EBRI tabulations of the May 1979 Current Population Survey.

1/ Totals and percents may not sum exactly due to rounding.

Table 3 shows that in 1979, there were about 1.1 million workers, ages twenty-one to twenty-four who were working for an employer with a pension plan but who were not participating in the plan. These workers had been with their employers for more than one year. Of these, approximately 500,000 were men and 600,000 were women. Between 85 and 87 percent of the male and female employees in this group worked more than 1,000 hours annually.

TABLE 3

Workers Ages 21 to 24 in 1979 with Their Employers More Than One Year and Not Participating in Their Employers' Pension Plans by Hours Worked and Sex

	Men (millions)		Women (millions)		Total Men and Women (millions)	
Working less than 1,000 hours annually	.065	13.3% 1/	.092	14.3% 1/	.158	13.9% 1/
Working more than 1,000 hours annually	.425	86.7	.553	85.7	.978	86.1
Total 1/	.491	100.0%	.645	100.0%	1.136	100.0%

Source: EBRI tabulations of the May 1979 Current Population Survey.

1/ Totals and percents may not sum exactly due to rounding.

Reducing the participation standard to age twenty-one would have increased the pension participation rate among women by approximately 1.4 percent in 1979. It would have increased the rate among men by 0.8 percent. This would have resulted in less than 1 million new participants.

Many believe that the costs of government regulation such as the Employee Retirement Income Security Act (ERISA) produce disincentives for new pension plan creation and incentives for plan termination. Thus, lowering participation standards, could result in a counterproductive response. For example, under current participation standards, there were 1.1 million new participants in newly qualified defined contribution plans and another 1.0 million new participants in newly qualified defined benefit plans in 1979. Plans newly qualified in 1980 and 1981 had 3.6 times as many participants as those established in 1979. In 1982, newly qualified defined contribution plans had 1.4 million participants, and newly qualified defined benefit plans had 1.3 million participants. The new plans have resulted in more than twice as many new participants as the number that would have resulted by reducing the pension participation age to twenty-one.

There is another consideration that is frequently overlooked. Reducing pension participation standards to age twenty-one could raise overall pension participation rates by 1 percent, but this does not mean that there would be a commensurate increase in pension benefit receipt or in benefit levels. ERISA provides that years of service beyond age twenty-two are to be counted for vesting purposes, regardless of a pension plan's actual participation standard. Additionally, some plan sponsors provide retroactive service credits once a worker reaches age twenty-five. In part, such credits may not be granted prior to that time in order to delay funding of the credit. More often, however, the credit is delayed to cut unnecessary administrative costs that would result from the high turnover rates among young workers.

Again, the 1979 survey data numbers are instructive. Under an age twenty-one participation provision, 978,000 young workers would have become new participants. If half of these workers ultimately vest under their current plan, there would be only 489,000 new persons who would ultimately receive benefits. If one-fourth vest, only 245,000 additional persons would receive benefits. Vesting rates show that 30 to 40 percent of the thirty-one- to thirty-five-year-old pension participants were vested in 1979. We can assume that the 30 to 40 percent rate represents an outside estimate of the twenty-one- to twenty-four-year-old 1979 nonparticipants who can be expected to vest by 1989. Those who will vest under an age twenty-one participation standard would probably vest under current ERISA standards. In other words, somewhere between one-fourth and one-half million, or 2 to 4 percent of the twenty-one- to twenty-four-year-olds may get slightly higher benefits under lower participation standards. This represents about 0.7 percent of all pension plan participants.

Reducing the pension participation age to twenty-one would entail numerous administrative changes. The important question that policymakers should consider is whether the small benefit gain is worth the substantial increase in pension administrative burdens.

Changing Break-In-Service Provisions

Generally, a "break in service" occurs when a plan participant has 500 or fewer hours of service with an employer in a "computation period." The computation period is twelve months--it may be a calendar year, a plan year or the twelve-consecutive-month period used to measure years of service.

Under ERISA, no benefit "accrues" during the break-in-service period. Thus, current accrual is foregone during a break in service. Nonvested past accruals are also sometimes lost. For a nonvested worker, a break in service means complete forfeiture of past accrued benefits, unless his break-in-service period is shorter than his prebreak service. "Vested" benefits, however, are protected. Additionally, all of the prebreak and postbreak service of a partially vested employee who has returned to work for one full year after a break in service are combined to determine his position on the vesting schedule.

The Retirement Equity Act (S. 19) would change the treatment of maternity and paternity leave for purposes of determining a break in service. Up to 501 hours of maternity or paternity leave would be counted as hours of service for purposes of determining whether a break in service occurred. The Economic Equity Act (S. 888/H.R. 2090) goes somewhat further than S. 19. This proposal would deem that employees on approved maternity or paternity leave have performed twenty hours of service per week for up to fifty-two weeks. Thus, S. 19 provides that no break in service has occurred for those on maternity and paternity leave for up to one year; and S. 888/H.R. 2090 provides for service credits and pension accruals during the one-year leave period.

A fundamental question which must be answered before such new legislation is put into effect is: Does maternity leave result in significant loss of service credits under present law? We can assist in developing answers to this latter question by using Social Security and Current Population Survey data.1/

For this analysis, we focused on women ages thirty-five to forty-four, who were working in May 1979, and who indicated that they had been with their employers for five or more years. There were roughly 2.4 million women in this group; they represented nearly one-third of all thirty-five- to forty-four-year-old working women. For women who had been with their employers prior to age twenty-two, only the years after their twenty-second birthdays were considered.

This age-group of women was chosen because they were nearing the end of their childbearing years; alternatively, if a younger group had been chosen, the recorded tenure would have fallen substantially. The five-or-more-year tenure criterion was selected, because any breaks in service for this group could have had a direct effect on their vesting status.

Table 4 shows the distribution of these women by tenure and work pattern. Over 80 percent had worked in their current jobs in every year over their reported tenure. This ranged from about 90 percent for those in jobs five to nine years, to about 75 percent for those in jobs fifteen or more years. In addition, 6 to 15 percent of these women had worked in all but one year. The work pattern for most of these women was remarkably stable. Women with stable work patterns would gain little, if anything, from the pending bills.

To assess the potential gains under the two bills, we simulated current break-in-service provisions for the women under analysis using the 1979 Current Population Survey matched with Social Security historical earnings data. We checked the frequency with which their breaks in service exceeded their prior years of service in their current jobs. In the 4,300 records, representing 2.4 million workers, we did not find a single instance where the breaks in service exceeded the prebreak service. One reason for this finding is that a relatively low-earnings level can produce a quarter of Social Security credit. For example, in 1977, $1,000 of covered earnings could result in four quarters of credit.

TABLE 4

Tenure and Work Patterns of Women Ages 35 to 44 During 1979

Work Patterns	Tenure with Current Employer: 5-9 Years	10-14 Years	15 or More Years
Worked every year	90.3%	82.8%	74.3%
Missed 1 year	6.1	9.0	15.3
Missed 2 years	1.8	4.4	0.0
Missed 3 years	0.6	2.7	2.0
Missed 4 years	1.2	0.0	6.6
Missed 5 years	0.0	1.1	1.9

Source: EBRI tabulations of Social Security administrative data matched to March 1978 and May 1979 Current Population Surveys.

To make a somewhat more realistic simulation, we treated any year where there was less than four full quarters of Social Security credits as a break-in-service year. Only 5 percent of the women under analysis would have lost service credits under current break-in-service rules. A somewhat larger portion of these women probably would have lost service credits due to breaks in service than our simulation suggests. However, the stable work patterns of these women make vesting a high probability; this suggests that these women will benefit little from S. 19.

In a subsequent simulation, we computed nonwork periods over the specified tenure for the women under analysis. Fourteen percent had at least one year with no earnings in their current jobs. The maternity service credits that S. 888 and H.R. 2090 would provide could affect these workers.

An equity question will arise as a result of any requirement that service and benefit accrual credits must be provided during maternity and paternity leave. While having and raising a family is admirable, there are other important activities which also result in tenure breaks. It is one thing to require employers to provide for previously earned credits when a break in service occurs; it is another to require that employers, in certain instances, must provide their employees with benefit accruals during such breaks.

Other Potential Policy Options

If reducing participation standards or adjusting break-in-service provisions will not result in significantly greater pension benefits for most women, we must examine whether other options can achieve these goals. In exploring such options, policymakers should understand that any potential legislation will affect various groups of women differently. EBRI's June Issue Brief showed that the work patterns of older women were considerably different than the work patterns of younger women. Because older women have already reached or are nearing retirement age, little or nothing can be done to affect their early career accruals.

Better communication and utilization of joint-and-survivor options can improve older women's retirement income security. Information on current joint-and-survivor utilization rates is scarce, but it is generally believed that many old-age widows are without benefits. The prevalence of life insurance coverage among pension participants, as part of a diversified benefits package, may make the low rates of joint-and-survivor selection less of a problem than is commonly believed, however. Increasing the tax-deductible limits of employer-provided life insurance may produce greater retirement income security for surviving widows than the joint-and-survivor provisions of pending legislation.

The current system provides equal pension opportunities for both men and women. To the extent younger women experience stable, enduring work patterns, they will acquire more substantial work-related pensions. For women with erratic and part-time employment, the likelihood of accruing a meaningful pension is small even under proposed legislative changes. Such a work pattern, however, will also result in low Social Security primary benefit entitlement. Social Security actuaries predict, however, that by 2010, when the baby-boom generation begins to retire, only 10 percent of retired worker beneficiaries will have spouses who receive dependent benefits. The increases in women working outside the home will result in an expanded number of women with entitlement to larger Social Security and pension benefits.

Some analysts focus on current pension recipiency levels among older women; they then look for pension policy adjustments that will make pensions more effective for women in general. A frequently proposed option would reduce ERISA's vesting standards. This option is primarily attractive to those who confuse the stability of the common defined benefit plan formula with the actual pattern of benefit accrual in these plans.

To show the difference, we simulated a hypothetical plan. The plan provided 1.5 percent of final-three-year-average salary for each year of credited service. Benefits were payable at age sixty-two for a set of hypothetical workers with different earnings and career patterns. We assumed 5 percent inflation and tested a range of real wage growth patterns. We also assumed retirement benefits were not indexed--an assumption with no practical effect on accrual patterns. Finally, we assumed a 7 percent discount rate for purposes of calculating the present value of benefits at various ages.

Table 5 reflects our simulation results. Two things are apparent. First, the largest retirement income accruals occur in the last five to ten years of a career, regardless of entry age. Second, the older a worker is when first employed, the larger his accruals will be during his early years under the plan. Moving to three- or five-year vesting in defined benefit plans will result in minimal benefit accruals for young workers.

Let us assume that: (1) participation standards are reduced to age twenty-two; (2) vesting standards are reduced to five years; and (3) the cash-out option is adjusted to include all benefits of less than $3,500 value. Under these assumptions, the overwhelming majority of workers who become eligible for additional benefits would receive a cash distribution. If these cash distributions were rolled over into individual retirement accounts (IRAs), then a marginal increase in retirement income security would result.

TABLE 5

Patterns of Benefit Accruals under a Hypothetical Defined Benefit Pension Plan for Various Workers at Specified Ages in Employment and Retiring at Age 62

Age at	Percent of Ultimate Benefit Value Accrued at the End of:						
Employment	5 Years	10 Years	15 Years	20 Years	25 Years	30 Years	35 Years
22 1/	0.1-0.2%	0.4-0.6%	1.4-1.6%	4.0%	9.5%	21.3%	46.6%
32	0.4-0.7	2.0-2.7	6.6-7.6	18.6-18.9	44.4	100.0	-
42	2.3-3.8	10.6-14.2	35.8-40.0	100.0	-	-	-
53	22.1-26.6	100.0	-	-	-	-	-

Source: Computed by the author. See text for assumptions.

1/ Assumes service credits from age twenty-two.

There is no evidence, however, suggesting that such rollovers occur regularly. EBRI's own experience is that most workers who leave with cash distributions do not roll them into alternative retirement income vehicles. The May 1983 Current Population Survey data, gathered by the Census Bureau, through the support of EBRI and the Department of Health and Human Services, will help to ascertain the extent of such cash distributions and their use.

Some analysts argue that under defined contribution plans, benefits accrue more evenly over the course of one's career than the benefits under defined benefit plans. Some believe that converting defined benefit plans to defined contribution plans and implementing shorter vesting standards would result in more equitable pension benefits and a more efficient pension system. These arguments are based on preconceived notions and assumptions about personal behavior; they are not based on fact.

If the lifetime work, earnings pattern, inflation and rate of return are known or assumed for a specific individual beginning a career, then a defined contribution plan can be designed to provide similar retirement benefit levels as those provided under a defined benefit plan. Few of us know the pattern our careers will take in advance. Let us assume, however, that this information is known. Then we can design a defined benefit and a defined contribution plan to provide equal benefits at the end of a full, forty-year career. This will permit us to compare the different experiences of workers with alternative career patterns under the two plans.

In most instances, workers entering these plans at early ages and leaving after ten years will be better off under the defined contribution plan. For such workers, the value of accumulated benefits under defined contribution plans could easily be five times the value of accumulated benefits under defined benefit plans. Upon plan withdrawal, vested defined contribution plan benefits usually can be cashed out. Vested defined benefit plan benefits usually will not be payable until retirement. When the cashed-out amount is rolled over into IRAs, young workers make significant progress toward their retirement income security. If they buy cars, take vacations or pay off bills, however, there is no direct contribution toward retirement income security.

Workers entering plans in middle-age will have a somewhat different experience. If they are in the plan for ten years, they will still receive a higher benefit under the defined contribution plan than under the defined benefit plan. The value difference between the defined contribution plan benefits and the defined benefit plan benefits, however, will be much smaller. The defined contribution benefits will be 1.5 to 2.0 times the value of defined benefit plan benefits at withdrawal. Alternatively, for the middle-age entrant who remains in the plan until <u>retirement</u>, benefits under the <u>defined benefit plan</u> can be as much as 26 percent greater than they would be under the defined contribution plan.

Workers who enter at early ages and stay throughout their careers may have somewhat different experiences under defined benefit and defined contribution plans--even though the plans are designed to provide comparable benefits. Defined benefit plans generally link benefits to final salary; thus, benefits are not dependent on investment experience. Defined contribution plan benefits do reflect investment experience. Plans sometimes experience unexpectedly high rates of investment return, but they may also experience negative or low returns. Under defined contribution plans, two workers with nearly identical careers and retirement plan contributions could receive very different benefit levels merely because they reach retirement age a couple of years apart from one another. A worker retiring when the market is at its peak could have an annuity that is 50 percent greater than a worker who retires two years later during a market trough. Under defined benefit plans, workers are insulated from such market variations.

Workers may prefer one plan over another because they anticipate a career pattern that will result in greater benefit receipt under a specific plan type. In terms of our concern with providing more pensions to more women, one plan will produce more benefits for some women, another plan will produce more benefits for other women. The prevailing characteristics of female work patterns today, however, suggest that many women will receive greater benefits under defined benefit plans that target accruals toward the end of their careers.

Formulating Pension Policy without Adequate Information

A frustrating aspect of the pension policymaking process is the insufficient information available to analyze current policies and legislative options. To an extent, more information exists than is used in analyzing policy issues. Two examples can be cited.

First, ERISA requires extensive disclosure of information on private pension levels. It also requires detailed statements on plan liability and funding status. Finally, ERISA requires detailed disclosure of the types of assets in pension portfolios. We estimate that private-sector employers pay as much as $100 million annually to cover the costs of ERISA's disclosure requirements.

If the government produced and edited statistical samples of the disclosed information and if these data were publicly available, analysts could trace the United States pension system's evolution. They could monitor long-term pension growth trends and the effects of economic cyclical variations and structural changes on plan participation and funding levels. The impact of financial market variations, inflation and other economic variations on the financial health of pension plans could be better understood.

Such information is presently not available. A couple of years ago the Internal Revenue Service (IRS) developed a sampling and editing system to provide these data on a timely basis. They developed a public use file of the 1977 plan year reports which EBRI, for example, used extensively in developing public policy research. No subsequent annual files have been made available nor does IRS have the funding to implement such a program.

Second, in 1978, Arthur Young and Company, under contract to the Department of Labor (DOL), collected program data from a sample of about 400 private pension plans with approximately 600,000 beneficiaries. This pension beneficiary data was matched to Social Security record data. While DOL has released no research reports utilizing this information, such reports could compare average 1978 pension benefits, produced from actual records, with actual Social Security benefits. Similar information is available on survey data sets, but in this case, underreporting is a serious problem.

These matched data are the richest known information source showing combined Social Security and pension income. They could provide a more comprehensive and accurate understanding of pension recipient income levels than any of the survey data currently used. Over the past two years, the DOL researchers and various contracted analysts have studied this information, but the data have not been made publicly available.

DOL is concerned about releasing such information to private analysts, since it has been matched to confidential Social Security records. The Social Security information is virtually identical in nature to the data matched with the 1978 Current Population Survey, however, which is publicly available and which has formed the basis for much of this analysis. Congress could improve this situation by clarifying the restrictions in the Tax Act of 1976 that limit the use of these data for research.

Due to a lack of pension information, policy deliberations often are influenced by misleading information. For example, Senator Mark O. Hatfield in introducing S. 918 on March 24, 1983 stated: "In fact, only 21 percent of women workers are covered by pension plans compared to 49 percent of men."2/ The May 1979 Current Population Survey showed that 15.0 million women, out of 39.2 million working women, participated in pension plans in 1979. Thirty-eight percent of working women participated in a plan. Another 5.6 million or 14 percent of working women were covered by plans, but they were not yet participants. Among women who were between the ages of twenty-five and sixty-four and who had been with their employers for more than one year, 61.8 percent participated in a pension plan. If Senator Hatfield's estimate of working women covered by pension plans was based on participation rates, it was off by 81 percent. If he was referring to coverage rates, the estimate was 148 percent off.

As the Congress concerns itself with pension policy issues, it may want to address the serious problem of information gaps. Many pension policy professionals are concerned that policy is being deliberated without essential statistics. Without such information, the potential exists for ill-advised, ineffective and wasteful policies. This could harm intended beneficiaries and the entire nation. It could increase employer costs and consumer prices; and it could decrease our nation's competitive strength. This may result in fewer jobs, lower tax revenues and increasing welfare expenditures.

Notes

1/ For an explanation of this data, see EBRI's Issue Brief, "Women and Pensions: Implications of a Maturing Pension System and Changing Female Work Patterns," no. 19 (June 1983).

2/ Bureau of National Affairs, Inc., BNA Pension Reporter, 4 April 1983, p. 607.

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