

# *The 1999 Small Employer Retirement Survey: Building a Better Mousetrap Is Not Enough*

by Paul Yakoboski, Pamela Ostuw, and Bill Pierron, EBRI

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*Issue Brief*

- As of 1995, there were 5.3 million small-employer firms (100 or fewer employees) in the United States. These small firms employed 38.0 million individuals, representing 38 percent of all employment. Therefore, low retirement plan coverage among small employers directly affects a sizeable fraction of the national work force.
- There are a number of reasons why more small employers do not offer retirement plans. Cost and administration-related issues do matter, but for many small employers these take a back seat to other issues. For some, the main driver is the financial reality of running a small business: Their revenue is too uncertain to commit to a plan. For others, the most important reasons for not sponsoring a plan are employee-related, e.g., the workers do not consider retirement savings to be a priority, or the employer's work force has such high turnover that it does not make sense to sponsor a plan.
- Many nonsponsors are unfamiliar with the different retirement plan types available to them as potential plan sponsors, especially the options created specifically for small employers. For example, most nonsponsors said they have never heard of (36 percent) or are not too familiar with (20 percent) SIMPLE plans for small businesses.
- Fifteen percent of small employers report that they are very likely to start a plan in the next two years, while 24 percent say this is somewhat likely.
- Nonsponsors report that the two items most likely to lead to serious consideration of sponsoring a plan are an increase in profits (69 percent) and business tax credits for starting a retirement plan (67 percent).
- Major drivers of low retirement plan sponsorship among small employers are who they employ and the uncertainty of revenue flows. While issues of administrative cost and burden matter, they are only part of the puzzle. Therefore, the solution is not simply "build it and they will come," by creating simpler and simpler retirement plans geared to small businesses. Rather, it is build it and they will come once the business reaches a certain level of profitability and stability, and once retirement planning and saving are more of a priority for the small employer's workers.

Paul Yakoboski, Pamela Ostuw, and Bill Pierron of EBRI wrote this *Issue Brief* with assistance from the Employee Benefit Research Institute's research and editorial staffs. Any views expressed in this report are those of the authors and should not be ascribed to the officers, trustees, members, or other sponsors of EBRI, EBRI-ERF, or their staffs. Neither EBRI nor EBRI-ERF lobbies or takes positions on specific policy proposals. EBRI invites comment on this research.

## Table of Contents

Introduction .....	3
Small Business Benefits .....	4
(chart 1)	
Employers Without Plans .....	4
Reasons for Not Offering a Plan .....	4
(table 1)	
Impact of Not Offering a Plan .....	5
(chart 2)	
Small Employers With Plans .....	6
(chart 3)	
Reasons for Offering a Plan .....	6
(table 2)	
Impact of Offering a Plan .....	6
(chart 4)	
Comparative Profiles .....	7
(table 3)	
Plan Knowledge .....	8
(chart 5, chart 6a, chart 6b)	
Motivating Plan Sponsorship .....	9
(chart 7)	
Implications .....	12
Conclusion .....	12
Appendix I: SERS Methodology .....	13
Appendix II: Current Legislative Proposals .....	14
The Secure Assets for Employees (SAFE) Plan Act .....	14
The Pension Coverage and Portability Act .....	14
Comprehensive Retirement Security and Pension Reform Act .....	14
Retirement Savings Opportunity Act .....	14
H.R. 352 .....	15
Income Security Enhancement Act of 1999 .....	15
Retirement Security Act of 1999 .....	15
Small Business Pension Start-Up Credit Act of 1999 .....	15

Employee Pension Portability and Accountability Act of 1999 .....	15
Appendix III: SERS Fact Sheets and Small Biz Retirement Quiz .....	16
Small Employers Without Plans .....	16
Small Employers With Plans .....	17
Small Biz Retirement Quiz .....	18
Appendix IV: Resources for Small Employers .....	19

## Tables

Table 1, Reasons for Not Offering a Retirement Plan .....	5
Table 2, Reasons for Sponsoring a Retirement Plan .....	7
Table 3, Company Demographics Among Small Employers With Retirement Plans and Those Without Plans .....	8
Table 4, Small Biz Retirement Quiz Scores .....	11

## Charts

Chart 1, Benefits Provided by Small Employers With and Without Retirement Plans .....	4
Chart 2, Impact of Not Offering a Retirement Plan to Employees (Non Plan Sponsors) .....	6
Chart 3, Types of Defined Contribution Plans Offered by Small Employers .....	7
Chart 4, Impact of Offering a Retirement Plan to Employees (Plan Sponsors) .....	8
Chart 5, Familiarity With Retirement Plan Options Among Small Employers Without Retirement Plans .....	9
Chart 6a, Beliefs About Retirement Plans Among Small Employers With a Plan .....	10
Chart 6b, Beliefs About Retirement Plans Among Small Employers Without a Plan .....	10
Chart 7, Factors That Might Lead to Plan Sponsorship Among Small Employers Currently Without a Plan .....	11

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## Introduction

The voluntary retirement system in the United States has been a success for workers at large

employers: According to Employee Benefit Research Institute (EBRI) tabulations of the Current Population Survey (CPS), 85 percent of workers at employers with 100 or more employees have an employer or union that sponsors a retirement plan. But this success is not shared by workers at small enterprises (fewer than 100 employees), where 31 percent of individuals have an employer or union that sponsors a retirement plan. Furthermore, less than one-half (46 per-cent) of full-time employees and only 13 percent of part-time employees in small private establishments (with fewer than 100 workers) actually *participated* in some type of employment-based retirement plan in 1996, according to the most recent data available from the U.S. Bureau of Labor Statistics (BLS).<sup>1</sup>

Why does this matter? Simply put, small employers are a big part of the U.S. economy. As of 1995, there were 5.3 million small-employer firms (100 or fewer employees) in the United States, accounting for 98 percent of all employers. These small firms employed 38.0 million individuals, representing 38 percent of all employment in the nation.<sup>2</sup> Therefore, low retirement

plan coverage rates directly affect a sizeable fraction of the work force, and lack of a retirement plan at work is a major reason why many individuals do not save for their retirement.

In June of 1998, the president and congressional leaders convened the first National Summit on Retirement Savings to discuss ways to better help Americans prepare for their retirement years. One of the main issues discussed by Summit delegates was the low retirement plan coverage rate among workers at small employers. This issue remains at the forefront of retirement policy discussions today.<sup>3</sup>

It is an issue that policymakers have continually revisited over time, and yet the gap persists. Most recently, the Small Business Job Protection Act of 1996 created the savings incentive match plan for employees (SIMPLE), a simplified retirement plan with fewer administrative requirements, specifically for small businesses. Employers who employ 100 or fewer employees on any day during the year and who do not maintain another employment-based retirement plan can adopt SIMPLE plans.<sup>4, 5</sup>

In 1998, in conjunction with the National Summit, EBRI, the American Savings Education Council (ASEC), and Mathew Greenwald & Associates (MGA) conducted the first Small Employer Retirement Survey (SERS). This *Issue Brief* presents the results of the second annual SERS, conducted earlier this year.<sup>6</sup>

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<sup>1</sup> See U.S. Department of Labor, Bureau of Labor Statistics, "Employee Benefits in Small Private Industry Establishments, 1996," News Release USDL: 98-240, 15 June, 1998.

<sup>2</sup> Source: U.S. Small Business Administration, Office of Advocacy, based on data provided by the Department of Commerce, Bureau of Census (published in Statistical Abstract of the United States, 1998).

<sup>3</sup> For more information and a copy of the Final Report on the 1998 National Summit on Retirement Savings, go to the Summit's Web site at [www.saversummit.org/98summit.htm](http://www.saversummit.org/98summit.htm). Two additional National Summits are scheduled to be held in 2001 and 2005.

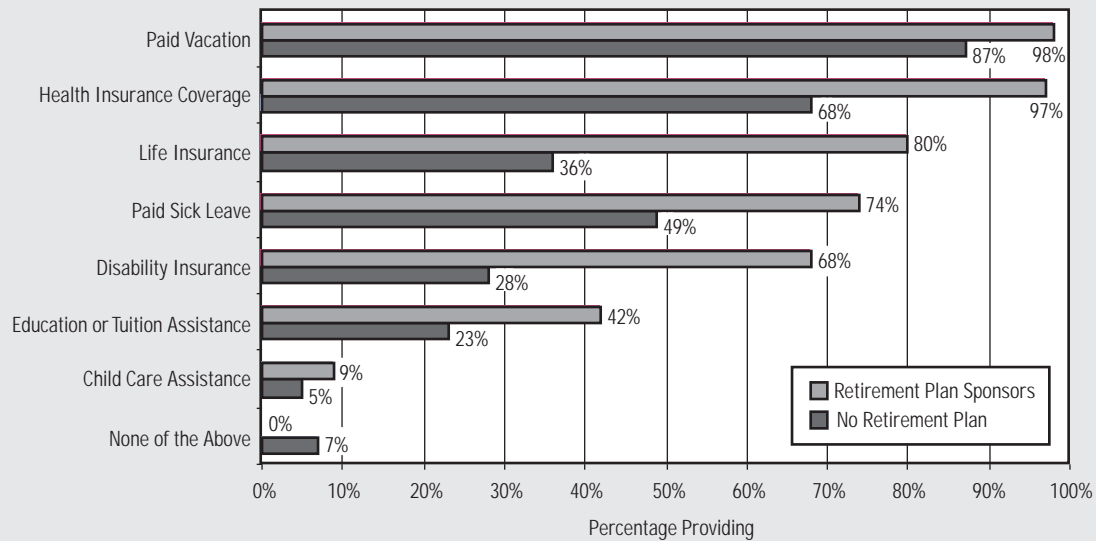
<sup>4</sup> A SIMPLE plan can be either an individual retirement account (IRA) for each employee or a 401(k) plan. SIMPLE 401(k) plans do not have to satisfy the special nondiscrimination tests applicable to regular 401(k) plans and are not subject to the top-heavy rules. All other qualified plan rules continue to apply. Within limits, contributions to a SIMPLE plan are not taxable until they are withdrawn. For a more complete discussion of SIMPLE plans, see

Appendix A in Fundamentals of Employee Benefit Programs, Fifth Edition (Washington, DC: Employee Benefit Research Institute, 1997).

<sup>5</sup> SIMPLE plans were not the first attempt to boost coverage in the small employer sector. The U.S. Congress sought to remove some of the burdens associated with administering a plan and complying with federal regulations in the Revenue Act of 1978, which established a new tax-favored retirement plan aimed primarily at small employers—the simplified employee pension (SEP). SEPs are arrangements under which an individual retirement account (IRA) is established for each eligible employee. The employee is immediately vested in employer contributions and generally directs the investment of the money. These arrangements are sometimes called SEP-IRAs. SEPs were designed to offer employers an uncomplicated alternative to more complex and costly qualified pension plans. They keep paperwork, record keeping, and reporting requirements to a minimum. For a more complete discussion of SEPs, see Fundamentals of Employee Benefit Programs, Fifth Edition (Washington, DC: Employee Benefit Research Institute, 1997).

<sup>6</sup> See Appendix I, SERS Methodology.

Chart 1  
Benefits Provided by Small Employers With and Without Retirement Plans



Source: Employee Benefit Research Institute, American Savings Education Council, and Mathew Greenwald & Associates, 1999 Small Employer Retirement Survey.

Conventional wisdom holds that low plan sponsorship rates among small employers are driven by high administrative burdens and costs placed on small employers. Findings from the 1999 SERS reveal that this view, while true for some small employers, is often too simplistic, and that the long-term solution to low coverage is not simply “building a better mousetrap” of new retirement programs. Plan nonsponsors responding to the survey report that employee-related reasons and revenue uncertainty are often more important reasons than red tape for not sponsoring a plan. This helps explain why actual coverage remains low, despite repeated public policy initiatives designed to boost retirement plan coverage among small employers. These issues, among others—such as changes that might lead to plan sponsorship and the motivations of small employers that offer a retirement plan—are examined in this *Issue Brief*. In addition, a listing is provided of legislative proposals aimed at improving small-employer retirement plan coverage (see Appendix II).

## Small Business Benefits

Many small employers do offer a variety of employee benefits to their employees

(chart 1). Data from the 1999 SERS show that small employers who offer retirement plans are also likely to offer paid vacation (98 percent), health insurance coverage (97 percent), and life insurance (80 percent) for

their employees. Nearly three-quarters (74 percent) of retirement plan sponsors with fewer than 100 employees offer paid sick leave to their employees, 68 percent offer disability insurance, and 42 percent offer education or tuition assistance. Child care assistance is offered least often by employers—only 9 percent of those with a retirement plan offer this benefit.

Among small employers who do not offer a retirement plan, many are still likely to offer other benefits to their employees. Eighty-seven percent of nonsponsors with fewer than 100 employees offer paid vacation benefits to employees, 68 percent offer health insurance coverage for employees, and 49 percent offer their employees paid sick leave. Thirty-six percent of small employer nonsponsors offer life insurance, 28 percent offer disability insurance, and 23 percent offer education or tuition assistance to employees. Five percent of small employers without retirement plans offer child care assistance as a benefit to their employees. Seven percent of nonsponsors do not offer any of the above benefits to their employees.

## Employers Without Plans

Reasons for Not Offering a Plan

There are a number of reasons why more small employers do not offer retirement plans—it is not simply a matter of administrative cost and burden. Cost and

Table 1  
Reasons for Not Offering a Retirement Plan

	Most Important Reason	Major Reason
Revenue is too uncertain to commit to a plan.	19%	50%
A large portion of workers are seasonal, part time, or high turnover.	19	42
Employees prefer wages and/or other benefits.	17	53
It costs too much to set up and administer.	12	30
Required company contributions are too expensive.	10	51
Too many government regulations.	3	32
Vesting requirements cause too much money to go to short-term employees.	2	38
Don't know where to go for information on starting a plan.	2	5
Benefits for the owner are too small.	1	17
Other reasons.	12	17

Source: Employee Benefit Research Institute, American Savings Education Council, and Mathew Greenwald & Associates, 1999 Small Employer Retirement Survey.

administration-related issues do matter, but for many small

employers they take a back seat to other issues. For some, the main driver is the financial reality of running a small business: Their revenue is too uncertain to commit to a plan. For others, the most important reasons for not sponsoring a plan are employee-related, e.g., the workers do not consider retirement savings to be a priority, or the employer's work force has such high turnover that it does not make sense to sponsor a plan (table 1).

Nineteen percent of nonsponsors said that the most important reason for not offering a plan was that revenue is too uncertain to permit the company to commit to a plan. One-half (50 percent) of all nonsponsors said that this was a major reason they do not sponsor a plan.

Having a large portion of workers who are seasonal, part time, or high turnover was cited by 19 percent as the most important reason for not sponsoring a plan. An additional 17 percent said employee preferences for wages and/or other benefits was the most important reason. Therefore, 36 percent of those without retirement plans cited some sort of employee-related reason as the most important reason for not offering a plan.

Twelve percent said the most important reason was that it cost too much to set up and administer a plan. Ten percent said the most important reason was that required company contributions are too expensive;<sup>7</sup>

<sup>7</sup> Plans exist in which employers as plan sponsors are not legally required to make contributions. For example, employer contributions are not required with a 401(k) plan—the sponsor could choose not to match participant contributions and to pass the administrative costs on to the plan. However, if the 401(k) is established as a SIMPLE plan, then company contributions are required.

<sup>8</sup> It is too soon to fairly evaluate the impact of SIMPLE plans on the small employer market.

3 percent said the most important reason was “too many

government regulations.” Therefore, 25 percent of nonsponsors cited a cost and/or administration-related reason as the most important reason for not offering a plan.

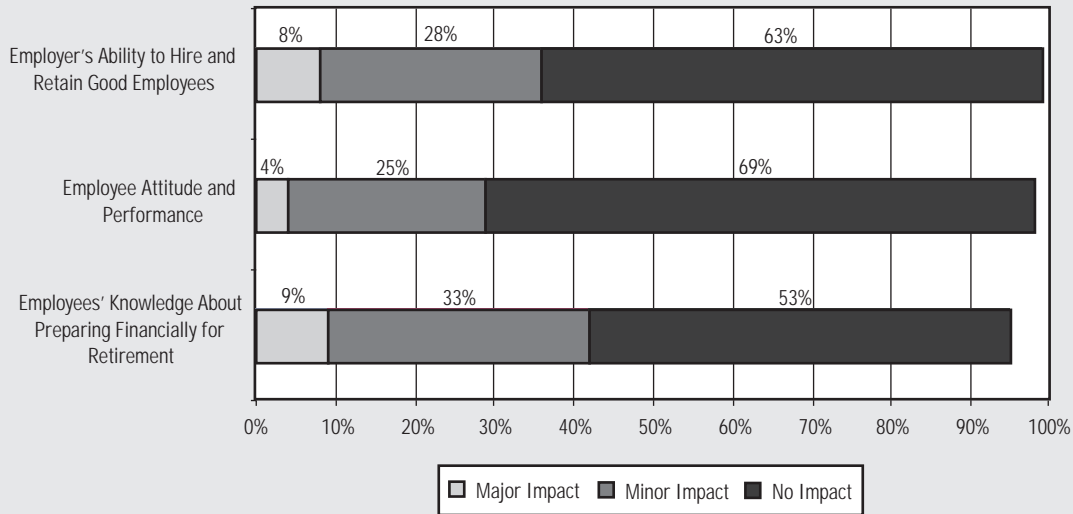
So, while cost and administrative issues do matter, they are not the sole reason for low plan sponsorship rates among small employers. In fact, based on small employer responses, they are not the *most important* reasons for the majority of nonsponsors: Employee-related reasons are most often cited as the most important factor for not offering a plan, and business profitability is also a main decision-driver. This may explain why plan sponsorship rates remain low despite repeated legislative efforts to boost them.<sup>8</sup>

## Impact of Not Offering a Plan

The majority of small employers without a retirement plan report that not offering a retirement plan to their employees has not affected their hiring or retention, employees' attitudes and performance, or employees' knowledge about preparing financially for retirement (chart 2). Sixty-three percent of small employers not offering a plan report that this had not had an impact on their ability to hire and retain good employees. Eight percent of nonsponsors said not having a retirement plan had a major impact on their hiring and retention of good employees, and 28 percent said it had a minor impact.

Sixty-nine percent of nonsponsors report that not having a retirement plan had no impact at all on their employees' attitude and performance, while 4 percent report it had a major impact and 25 percent report a minor impact. Just over half (53 percent) of nonsponsors believe that lack of a retirement plan has no impact on their workers' financial knowledge about preparing for

Chart 2  
Impact of Not Offering a Retirement Plan to Employees (Non Plan Sponsors)



Source: Employee Benefit Research Institute, American Savings Education Council, and Mathew Greenwald & Associates, 1999 Small Employer Retirement Survey.

retirement. Nine percent say it has a major impact, and 33 percent report a minor impact on their employees' knowledge about financially preparing for retirement.

## Small Employers With Plans

Small employers that do offer retirement plans are overwhelmingly likely (84 per-

cent) to offer their employees only a defined contribution (DC) plan that provides an individual account for each participant, based only on amounts contributed or allocated to the account. Two percent offer their employees only a defined benefit (DB) plan, the traditional type of pension plan that pays a specified amount based on a predetermined formula. Seven percent offer both DC and DB plans to their employees.

Among the small employers who offer their workers a DC plan, it is most likely a 401(k) plan (67 percent) (chart 3). About one-quarter of small employers with DC plans (26 percent) offer a profit-sharing plan. Eleven percent offer a SIMPLE plan, and 10 percent offer a 403(b) plan (for education and nonprofit organizations).

## Reasons for Offering a Plan

One-third of small employers (33 percent) report that the most important reason their business offers a retirement plan is the competitive advantage in employee recruit-

ment and retention (table 2). Slightly fewer (28 percent) say the most important reason for them is the positive effect on employee attitude and performance. Another 12 percent say that the most important reason their business offers a plan is that they believe employers have an obligation to provide a retirement plan for their workers. Tax advantages for employees, tax advantages for key executives, and employee demand are other reasons cited by small employers as reasons for offering retirement plans.

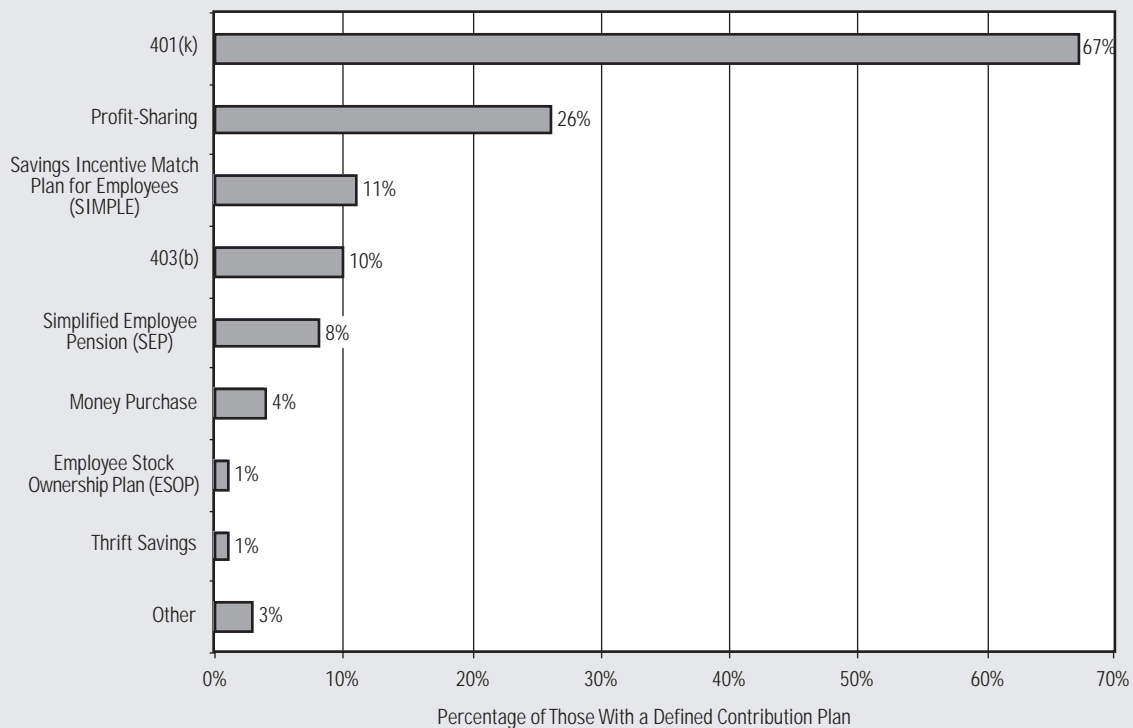
## Impact of Offering a Plan

Whereas small employers without retirement plans report that *not having* a plan has not affected their business (see above), small employers with plans report that *having* a plan has had a positive impact on their business (chart 4). Thirty-nine percent of small employers with plans report that having a plan has had a major impact on their ability to hire and retain good employees. An additional 45 percent report that having a plan has had a minor impact on their hiring and retention. Fifteen percent say there has been no impact.

A majority of small employers with plans report that having a retirement plan has had an impact on employees' attitude and performance (32 percent report a major impact and 52 percent report a minor impact). Fourteen percent say that having a plan has not had an impact on employee attitude and performance.

Fifty-three percent of plan sponsors say that having a plan has had a major impact on their employ-

Chart 3  
Types of Defined Contribution Plans Offered by Small Employers



Source: Employee Benefit Research Institute, American Savings Education Council, and Mathew Greenwald & Associates, 1999 Small Employer Retirement Survey.

ees' ability to prepare financially for retirement (37 percent report a minor impact). Six percent report that having a plan has not affected their employees' ability to prepare for retirement.

## Comparative Profiles

Small employers that sponsor retirement plans tend to be distinctly different from small

employers without plans, in terms of revenue levels and the composition of their work force. These findings are not surprising, given the results above; in fact, they bolster the conclusion that low coverage rates are driven by more than just issues of administrative cost and burden. The challenge posed by low coverage rates among small employers is deeper than that, since it is tied to the basic characteristics of small employers and their employees.

For example, small employers that offer retirement plans tend to have higher revenues than small employers that do not have retirement plans (table 3). Thirty-four percent of plan sponsors report that the approximate annual gross revenue of the company was

less than \$2 million for 1998, and nearly half (48 percent) report gross revenue of more than \$2 million. In comparison, 63 percent of employers without a plan reported annual gross revenues less than \$2 million for 1998, and just 18 percent reported gross revenues more than \$2 million.

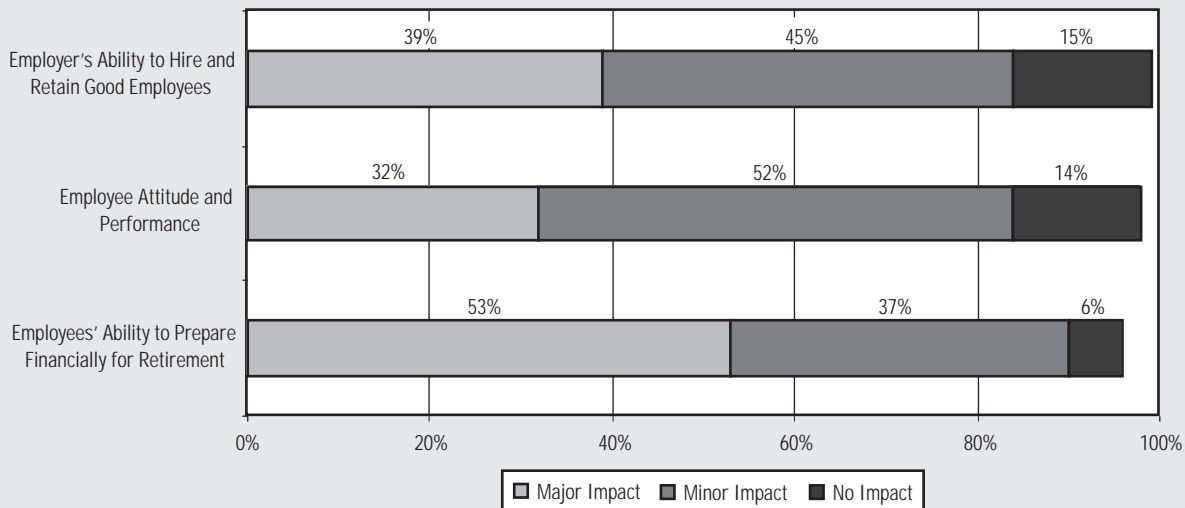
Small employers offering retirement plans tend

Table 2  
Reasons for Sponsoring a Retirement Plan

	Most Important Reason	Major Reason
Competitive Advantage in Employee Recruitment and Retention	33%	60%
Positive Effect on Employee Attitude and Performance	28	71
Employers Have an Obligation to Provide a Retirement Plan for Employees	12	29
Tax Advantages for Employees	7	38
Tax Advantages for Key Executives	6	25
Employees Demand or Expect It	5	21
Other	5	9

Source: Employee Benefit Research Institute, American Savings Education Council, and Mathew Greenwald & Associates, 1999 Small Employer Retirement Survey.

Chart 4  
Impact of Offering a Retirement Plan to Employees (Plan Sponsors)



Source: Employee Benefit Research Institute, American Savings Education Council, and Mathew Greenwald & Associates, 1999 Small Employer Retirement Survey.

to employ different types of workers than employers that do not—their employees tend to be older, have higher earnings, have more formal education, and remain with the company longer (table 3).

Small employers with retirement plans also tend to think their employees are better prepared for retirement. Sixty-three percent of plan sponsors say they think their employees are well prepared for retirement (9 percent very well prepared and 54 percent somewhat well prepared). However, among nonsponsors, 31 percent think their employees are well prepared (3 percent very well prepared and 28 percent somewhat well prepared).

## Plan Knowledge

Many nonsponsors are unfamiliar with the different retirement plan types available to them as potential

plan sponsors, especially the options created specifically for small employers (chart 5). Most nonsponsors said they have never heard of (36 percent) or are not too familiar (20 percent) with SIMPLE plans, one of the plan types created especially for small employers. The same holds for simplified employee pensions (SEPs). Forty-six percent of nonsponsors have never heard of SEPs and 24 percent say they are not too familiar with SEPs. By comparison, very few nonsponsors said they have never heard of or are not too familiar with 401(k) plans (3 percent and 12 percent, respectively).

In addition, many small employers simply lack

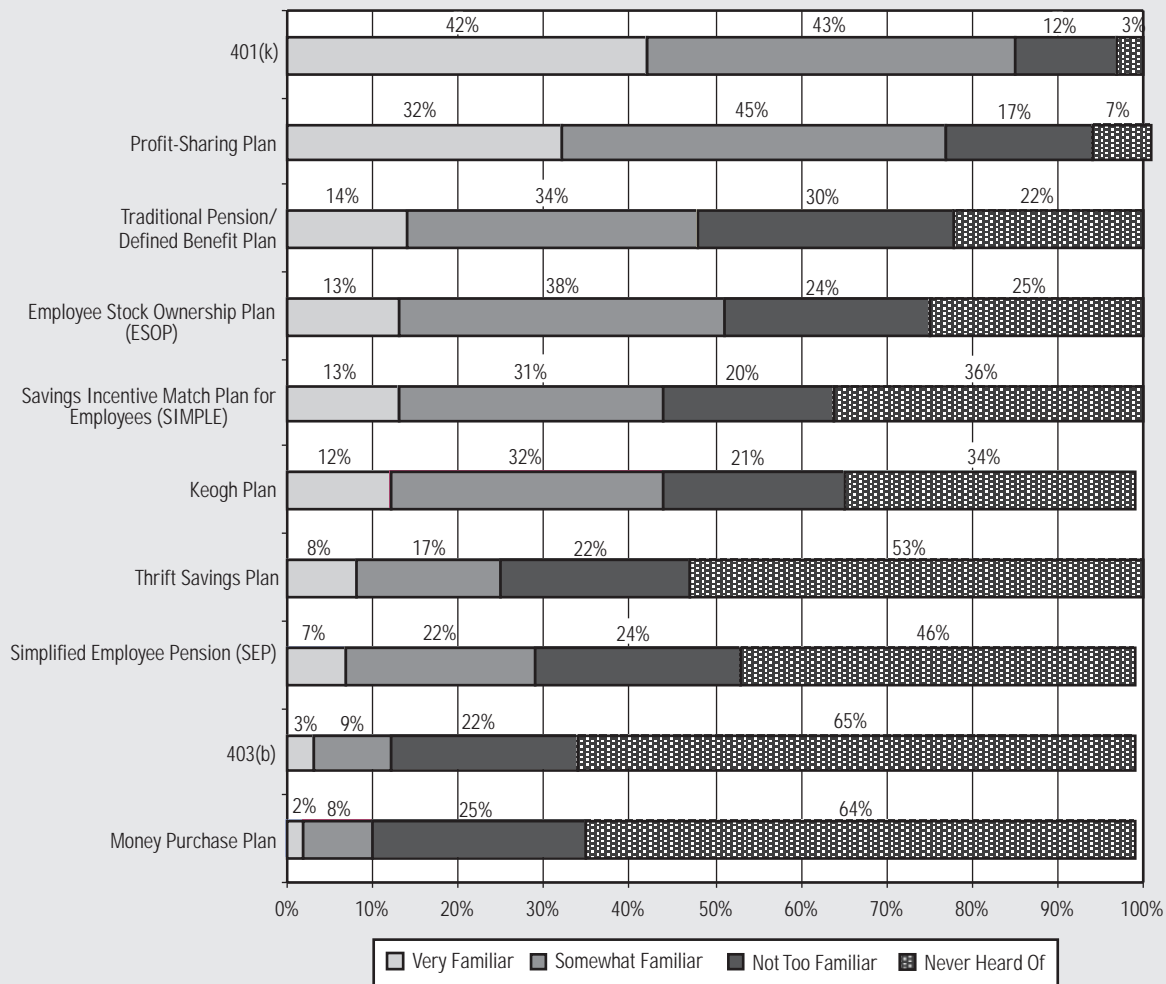
Table 3  
Company Demographics Among Small Employers With Retirement Plans and Those Without Plans

	Plan Sponsor	No Plan
Approximate Gross Revenue in 1998		
Less than \$2 million	34%	63%
\$2 million or more	48	18
Not reported	19	20
Age of Most Full-Time Employees		
Age 30 or younger	11	23
Age 30–39	62	51
Age 40 or older	24	25
Annual Salary of Most Full-Time Employees		
Less than \$20,000	9	32
\$20,000–\$40,000	73	58
\$40,000 or more	11	8
Educational Level of Most Full-Time Employees		
High school or less	41	58
Some college	35	31
College degree or more	20	9
Length of Time Most Full-Time Employees Stay With Company		
Less than 3 years	8	27
Between 3 and 9 years	56	45
10 years or more	31	24

Source: Employee Benefit Research Institute, American Savings Education Council, and Mathew Greenwald & Associates, 1999 Small Employer Retirement Survey.



Chart 5  
Familiarity With Retirement Plan Options Among Small Employers Without Retirement Plans



Source: Employee Benefit Research Institute, American Savings Education Council, and Mathew Greenwald & Associates, 1999 Small Employer Retirement Survey.

information, or are even misinformed, about retirement plan options and what plan sponsorship actually entails (charts 6a and 6b). The 1999 SERS contained a seven-question true/false “quiz” regarding retirement plan sponsorship (see Appendix III for the full quiz). The *Small Biz Retirement Quiz* covered topics such as the cost of sponsoring a plan, what an employer as a plan sponsor can do, and what a plan sponsor is required by law to do.

While there were some differences in overall scoring on the quiz between retirement plan sponsors and nonsponsors, it was not as great as some might expect (table 4). Twenty-six percent of plan sponsors and 19 percent of nonsponsors had six or seven correct answers on the *Quiz*. Sixty-two percent of plan sponsors and nonsponsors alike had three to five correct answers. Eleven percent of small employers with retirement plans and 19 percent of those without plans had zero to two

correct answers.

The findings indicate that, on deciding to sponsor a plan, a small employer then turns to the knowledge and expertise of an outside professional to implement and run the plan. So a lack of knowledge may not be as large a deterrent as the reasons discussed earlier—employers learn what they need to know when they need to know it. It is clear, however, that the majority of small employers without plans are largely unfamiliar with the plan options that have been created specifically for them. This probably changes when they decide to sponsor a plan, but not before.

## Motivating Plan Sponsorship

The potential exists for increased plan sponsorship among

Chart 6a

**Beliefs About Retirement Plans Among Small Employers With a Plan**

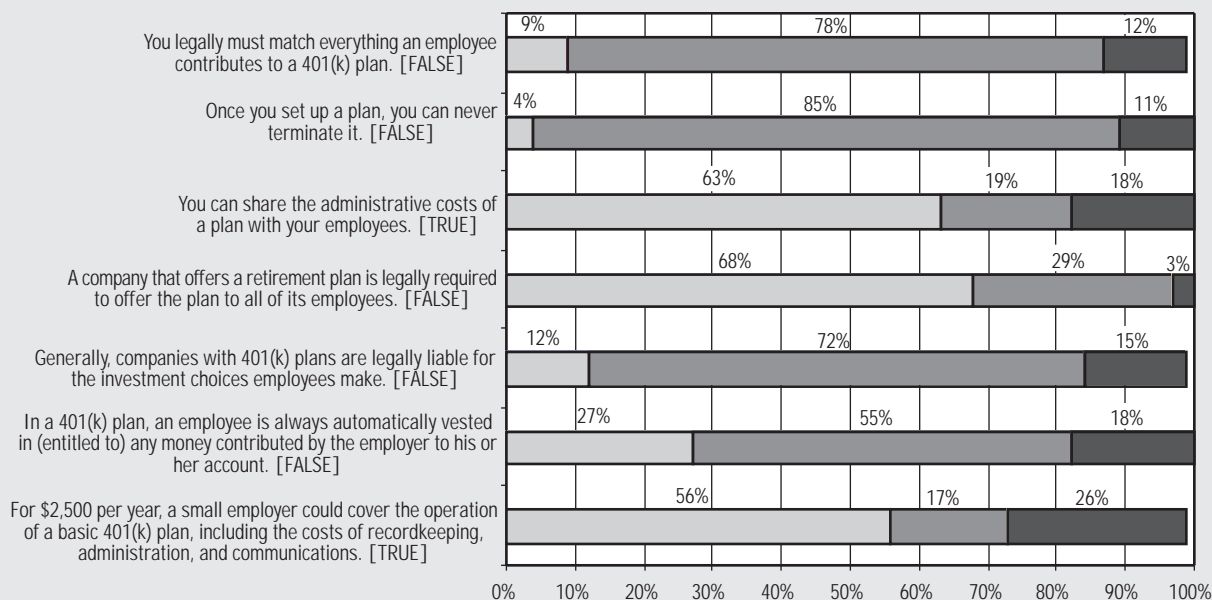
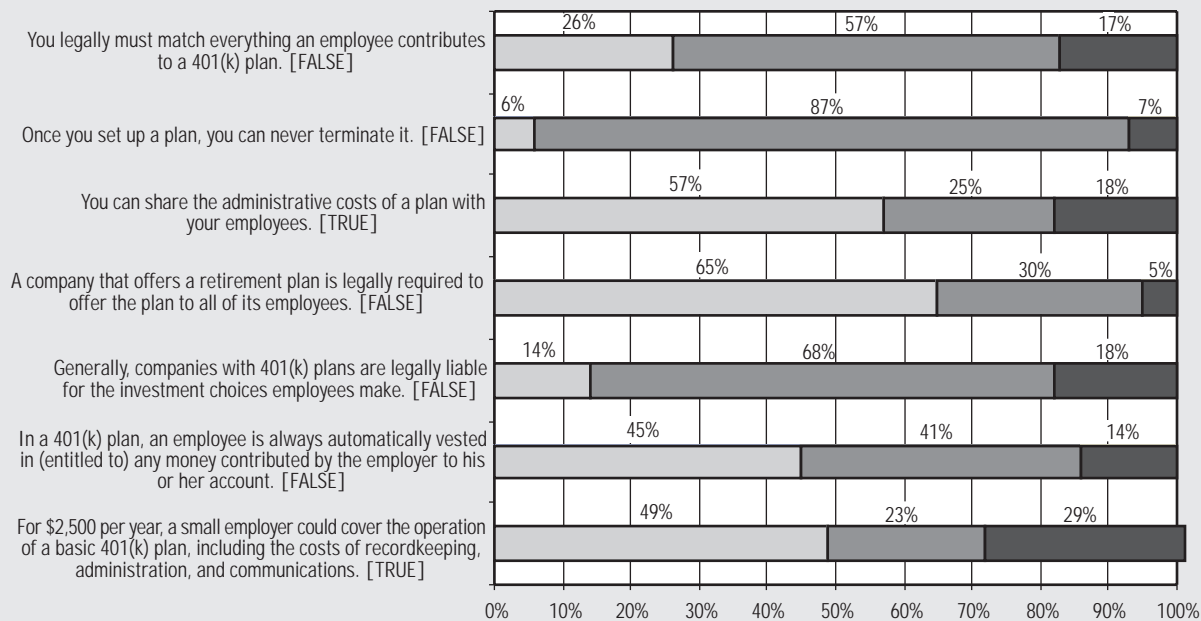


Chart 6b

**Beliefs About Retirement Plans Among Small Employers Without a Plan**



True False Don't Know

Source: Employee Benefit Research Institute, American Savings Education Council, and Mathew Greenwald & Associates, 1999 Small Employer Retirement Survey.

Table 4  
**Small Biz Retirement Quiz Scores**

	Plan Sponsor	No Plan
6 or 7 correct answers	26%	19%
3 to 5 correct answers	62	62
0 to 2 correct answers	11	19

Source: Employee Benefit Research Institute, American Savings Education Council, and Mathew Greenwald & Associates, 1999 Small Employer Retirement Survey.

small employers. Fifteen percent of small employers report that they are very likely to start a plan in the next two years, while 24 percent say this is somewhat likely. (Another 24 percent are not too likely to start a plan, and 36 percent are not at all likely to establish one.)

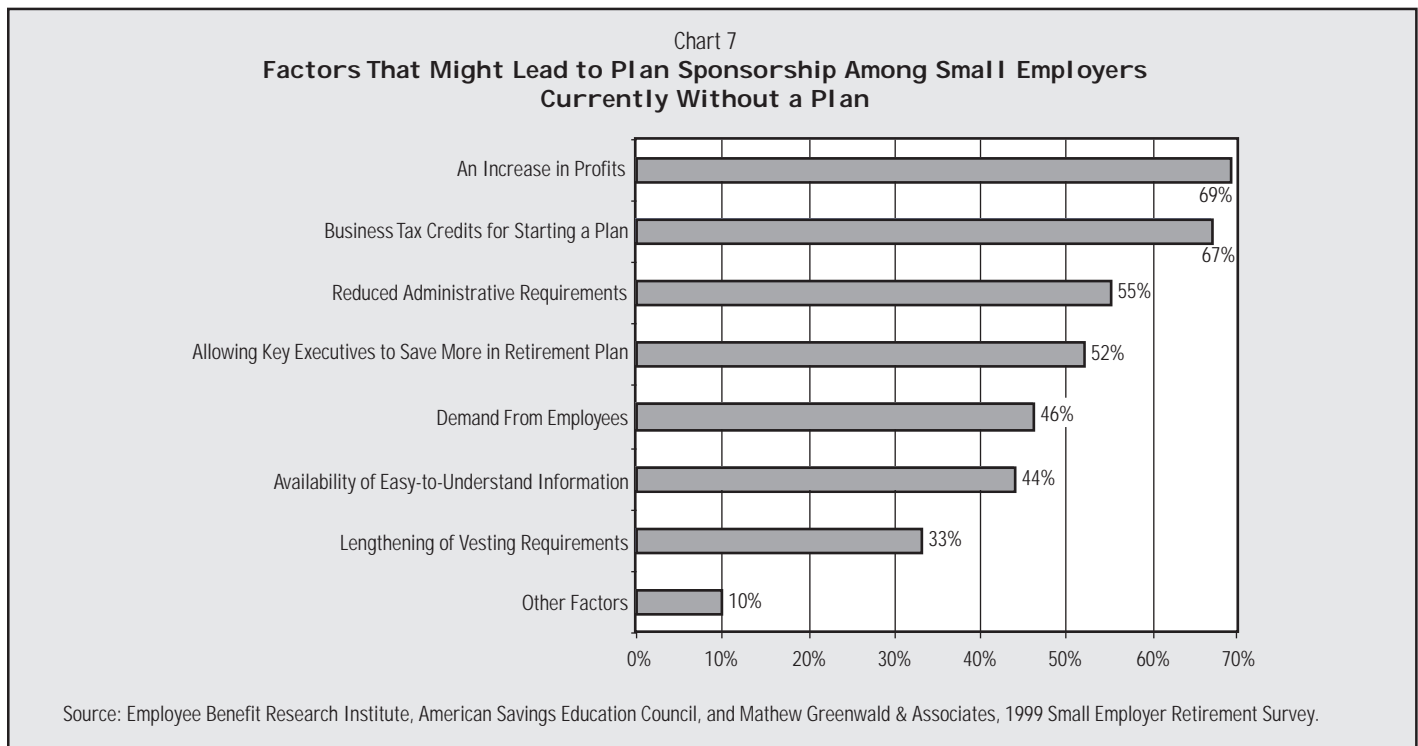
Those likely to start a plan are somewhat more likely to report that the most important reason they don't currently have a plan is revenue uncertainty, and are less likely to say it is because a large portion of their workers are seasonal, part time, or high turnover. It therefore appears that they feel continued improvement in their business conditions will allow them to start a plan within the next couple of years.

In addition, nonsponsors reporting that they are likely to start a plan in the next two years are generally more familiar with different plan types than are those not likely to start a plan.<sup>9</sup> They also score slightly higher, on average, on the *Small Biz Retirement Quiz*.

This provides some indication that their growing interest has led them to learn about the options available.

What, then, would lead to increased plan coverage? Nonsponsors were read a list of items and asked if any would make them seriously consider sponsoring a retirement plan (chart 7). Nonsponsors report that the two items most likely to lead to serious consideration of sponsoring a plan are an increase in profits (69 percent) and business tax credits for starting a retirement plan (67 percent). The latter may be viewed as substitute for the former, i.e., the government cannot improve the profitability of a business, but it could

<sup>9</sup> Ninety-one percent of small employers likely to start a plan in the next two years were very or somewhat familiar with 401(k) plans, compared with 81 percent of small employers not likely to start a plan. Similarly, 49 percent of those likely to start a plan and 40 percent of those not likely to start a plan were very or somewhat familiar with SIMPLE plans, and 39 percent and 22 percent, respectively, were very or somewhat familiar with SEPs.



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subsidize the costs of starting a retirement plan for a small employer's workers. The other responses were:

- Fifty-five percent would consider starting a plan if a plan with reduced administrative requirements were offered.
- Allowing key executives to save more in a retirement plan would affect 52 percent of nonsponsors.
- Demand from employees would influence 46 percent of nonsponsors.
- Availability of easy-to-understand information would influence 44 percent.
- Lengthening of vesting requirements would influence 33 percent.

## *Implications*

Major drivers of low retirement plan sponsorship among small employers are who they employ

and the uncertainty of revenue flows. While issues of administrative cost and burden matter, they are only part of the puzzle. Therefore, the solution is not simply "build it and they will come," by creating simpler and simpler retirement plans geared to small businesses. Rather, it is build it and they will come once the business reaches a certain level of profitability and stability, and once retirement planning and saving are more of a priority for the small employer's workers. It is at that point that the new vehicles created by policymakers specifically for small employers will begin to realize their full potential.

As the survey shows, 39 percent of small employers without plans say they are very or somewhat likely to start a plan in the next two years; with changes, this number could be expected to rise. Long-term solutions to increased coverage among small employers include: education of workers, so that they view retirement planning and saving as a personal priority and communicate their desire for a retirement plan to their employer; ongoing good economic conditions, so that business

profits and the affordability of plan sponsorship improves; or, as the survey indicates, policy changes such as simplification and tax credits that help make plans more affordable. This is not said to endorse any particular policy changes; rather, it is to make clear that, based on the survey responses of small employers, there are actions Congress could take to expand small-employer plan sponsorship.

## *Conclusion*

There are no quick fixes or "silver bullets" that will ensure American workers' retirement income

security, especially for those working for small employers. Findings from the 1999 SERS indicate that long-term policies aimed at improving workers' retirement income security must not only address employers' concerns about offering plans but also workers' needs for education and making retirement saving and planning a priority.

While conventional wisdom maintains that low plan sponsorship rates among small employers are driven by high administrative burdens and cost placed on small employers, the SERS findings reveal that this view of the world is too simplistic and often wrong, and that the solution to low coverage is not simply "building a better mousetrap." In fact, nonsponsors report that employee-related reasons and revenue uncertainty are often more important reasons for not sponsoring a plan. This helps explain why actual coverage remains low, despite repeated public policy initiatives designed to boost retirement plan coverage among small employers.

Given this finding, it is not surprising that there are notable differences between small employers that choose to sponsor a retirement plan and those that do not. In particular, the survey reveals differences in the characteristics of the workers employed by companies that sponsor retirement plans and workers employed by nonsponsors. Workers with demographics typically

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associated with a lesser degree of focus on retirement preparation—e.g., younger ages and lower incomes—account for a relatively greater share of employment at small employers that do not have a retirement plan.

Nonsponsors report that the two items most likely to lead to serious consideration of sponsoring a

plan are an increase in profits and business tax credits for starting a retirement plan. The latter may be viewed as substitute for the former, i.e., the government cannot improve the profitability of a business, but it could subsidize the costs of starting a retirement plan for a small employer's workers.

### 1999 SERS Underwriters

The 1999 Small Employer Retirement Survey (SERS) was underwritten by grants from the following organizations: American Society of Pension Actuaries, CIGNA Corporation, Edward Jones, Investment Company Institute, ManuLife Financial, Nationwide Life Insurance Co., Principal Financial Group, Prudential Investments, and T. Rowe Price Services, Inc.

## Appendix I

### SERS Methodology

The annual Small Employer Retirement Survey

(SERS), now in its second year, was designed to gauge the views and attitudes of America's small employers (with five to 100 full-time workers) regarding retirement plans and related issues. The survey was conducted within the United States between January 4 and February 28, 1999, through 15-minute telephone interviews with 301 companies with a retirement plan and 301 companies without a retirement plan. Within each sample, quotas were established to ensure adequate representation by size of business.

In theory, each sample of 301 yields a statistical precision of plus or minus 6 percentage points (with 95 percent certainty) of what the results would be if all businesses with five to 100 full-time workers were surveyed with complete accuracy. There are other possible sources of error in all surveys, however, that may be more serious than theoretical calculations of sampling error. These include refusals to be interviewed and other forms of nonresponse, the effects of question

wording and question order, and screening. While attempts are made to minimize these factors, it is difficult or impossible to quantify the errors that may result from them.

The SERS was co-sponsored by the Employee Benefit Research Institute (EBRI), a private, nonprofit, nonpartisan public policy research organization; the American Savings Education Council (ASEC), a partnership of more than 250 private- and public-sector institutions dedicated to raising public awareness of what is needed to ensure long-term personal financial independence, and part of the EBRI Education and Research Fund; and Mathew Greenwald & Associates, Inc. (MGA), a Washington, DC-based market research firm.

The 1999 SERS data collection was funded by grants from nine organizations: American Society of Pension Actuaries, CIGNA Corporation, Edward Jones, Investment Company Institute, ManuLife Financial, Nationwide Life Insurance Co., Principal Financial Group, Prudential Investments, and T. Rowe Price Services, Inc. Staff time was donated by EBRI, ASEC, and MGA. SERS materials, the *Small Biz Retirement Quiz*, and the list of underwriters may be accessed at the EBRI Web site: [www.ebri.org/sers](http://www.ebri.org/sers).

## Appendix II

### Current Legislative Proposals

The following legislative proposals are aimed, in whole or in part, at generating greater retirement plan sponsorship among small employers. These summaries are not meant to be comprehensive, and focus solely on the provisions of the bills that deal specifically with small-business retirement plans.

***The Secure Assets For Employees (SAFE) Plan Act***  
H.R. 2190, co-sponsored by Reps. Nancy Johnson (R-CT) and Earl Pomeroy (D-ND), would create a simplified defined benefit plan with the same eligibility and participation requirements as the SIMPLE defined contribution plan for businesses with 100 or fewer employees. In essence, SAFE is a cash balance pension plan with mandatory annuitization upon retirement. Benefits would be fully vested and portable upon job termination.

An employer sponsoring a SAFE plan would provide all eligible employees a benefit equal to 1 percent, 2 percent, or 3 percent of compensation for each year of service. Companies that experience revenue fluctuations could choose to cut the minimum benefit to 1 percent or 2 percent in a given year. The bill would also allow employers to credit employees for up to 10 years of past service. SAFE plan sponsors would not be required to pay premiums to the Pension Benefit Guaranty Corporation (PBGC), as do sponsors of defined benefit pension plans. Assets would have to be held in the form of insurance company annuities or in trust in certain specified investment products.

SAFE previously had been introduced in the last Congress as H.R. 1656, but this year's version of the legislation contains different actuarial assumptions. As introduced in 1997, H.R. 1656 specified that SAFE plans would be required to use a specified conservative actuarial assumption of a fixed 5 percent, to ensure the minimum retirement benefit. Under the current legislation (H.R. 2190), SAFE plans would be required to use specified conservative actuarial assumptions of 3 percent to 5 percent to ensure the minimum retirement benefit.

SAFE also has been included in S. 741, and S. 649 (see below).

***The Pension Coverage and Portability Act***

S. 741, co-sponsored by Sens. Bob Graham (D-FL) and Charles Grassley (R-IA), contains a number of provisions designed to simplify plan administration and encourage plan sponsorship and participation among small employers. Similar legislation (H.R. 1102, see below) has been introduced in the House by Reps. Rob Portman (R-OH) and Benjamin Cardin (D-MD).

The bill contains provisions aimed at providing relief to employers from the Sec. 416 "top-heavy" rules of the tax code. Under the rules, a plan is deemed top heavy if more than 60 percent of the accounts or accrued benefits under the plan are attributable to key employees. If so, the plan must satisfy tougher requirements for vesting and for contributions and benefits. The bill would modify how the 60 percent figure is calculated, to include only benefits accrued or contributions made in the prior year. The bill also would repeal the current requirement that the sponsor of a "frozen" defined benefit plan continue to make contributions on behalf of non-key employees.

The bill would reduce premiums for small employers whose defined benefit plans are insured by PBGC, cutting the premiums from \$19 per participant to \$5 during the first five years that a small-business defined benefit plan exists.

The bill also includes a start-up tax credit for small businesses that adopt plans; the SAFE defined benefit plan (see H.R. 2190); and elimination of Internal Revenue Service (IRS) user fees that new-plan sponsors must pay when they apply for IRS approval.

***Comprehensive Retirement Security and Pension Reform Act***

H.R. 1102, cosponsored by Reps. Rob Portman (R-OH) and Benjamin Cardin (D-MD), includes numerous provisions designed to simplify plan administration and encourage more small employers to offer plans.

The bill would modify the tax code's "top-heavy" rules by simplifying the definition of a key employee; streamline the deduction and reporting rules for small businesses (those with 100 or fewer employees); and eliminate IRS user fees for information requests regarding small business pension plans.

The bill would provide incentives for employers to establish tax-deferred salary reduction plans that automatically enroll employees, and would grant relief from "excessive PBGC premiums" for new small-business defined benefit plans.

The bill also would establish a \$2,000 tax credit for the establishment or administration of a new small business pension plan, or the retirement-related education of employees. The credit would amount to \$1,000 in the first year of plan operation and \$500 per year in the subsequent two years.

The bill would require the Treasury Department to issue "model" defined benefit and defined contribution plans for small employers to minimize regulatory costs and burdens.

***Retirement Savings Opportunity Act***

S. 649, co-sponsored by Sens. William Roth, Jr. (R-DE) and Max Baucus (D-MT), seeks to encourage greater retirement savings by increasing the contribution limits for qualified employment-based plans and individual

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retirement accounts (IRAs). The bill also would create so-called backloaded "Roth 401(k)" and "Roth 403(b)" plans (for education and nonprofit organizations) that would allow after-tax contributions and tax-free buildup and distributions. It also would include several provisions aimed at small employers.

The bill would provide a tax credit to small businesses with fewer than 100 employees for new plan start-up expenses of up to \$500 per year for each of first three years. For small businesses with fewer than 50 employees that set up new plans, the bill would provide a deduction of up to 50 percent of employer contributions for nonhighly compensated employees (NHCEs), up to an annual maximum of 3 percent of total NHCE compensation, for the first five years of operation. This NHCE credit would be available only if the employer had no qualified plan for the three preceding years.

The bill also would raise the contribution limit for SIMPLE plans from \$6,000 annually to \$10,000 annually. It also includes the SAFE defined benefit plan for small employers (see H.R. 2190).

#### ***H.R. 352***

H.R. 352, co-sponsored by Reps. Roy Blunt (R-MO) and Ken Bentsen (D-TX), is designed to simplify the process of establishing and administering small-business retirement plans by simplifying administration, raising contribution limits, and establishing tax credits for new plans. In essence, it modifies the current SIMPLE plan.

The bill would allow small firms to claim a tax credit of up to \$6,000 over five years to offset start-up and administrative costs of a retirement plan. The tax credit would provide \$2,000 in the year the plan is established, and up to \$1,000 per year for the subsequent four years. Administrative costs include the cost of establishing, administering, and maintaining the plan, as well as the cost of educating employees.

The bill also would relax pension administrative requirements, and would raise the contribution limits for small employer plans to \$10,000 per year or 25 percent of compensation, to coincide with the limits for non-SIMPLE 401(k) plans.

#### ***Income Security Enhancement Act of 1999***

S. 8, sponsored by Sen. Tom Daschle (D-SD), would create a tax credit for small employers that establish retirement plans. The credit would be available only to firms that did not maintain qualified plans during the previous year. Recipients would get a credit against income tax of 50 percent of the costs of establishing a qualified plan before 2002, with a maximum credit of \$1,000 in the first year after the date the plan is established and \$500 in the two subsequent years.

The bill also would allow small employers to adopt the Secure Money Annuity or Retirement Trust (SMART) Plan, a simplified defined benefit plan similar to the SAFE proposal (see H.R. 2190). SMART would

provide a minimum annual benefit equal to 1 percent or 2 percent of compensation (the employer could elect to provide a benefit of 3 percent of pay during first five years of the plan); prohibit employee contributions; and fully vest employees with two years of service and at least \$5,000 in earnings in current year.

SMART plans could be funded as an annuity or a trust invested in certain specified investment products, with excess investment returns, if any, credited to employees. SMART trust benefits would be guaranteed by PBGC at a reduced premium level.

The bill also would create a tax credit for small employers (100 or fewer employees) that establish pension plans. The credit would cover up to 50 percent of small employer pension plan start-up costs, with a limit of \$1,000 for the first year and \$500 for each of the second and third years.

#### ***Retirement Security Act of 1999***

H.R. 1590, sponsored by Rep. Sam Gejdenson (D-CT), is another comprehensive package of retirement plan provisions, some of which are designed to encourage small employers to offer retirement plans. The bill would establish the Secure Money Annuity or Retirement Trust (SMART) plan, like S. 8 (see above).

The bill would create a tax credit for small employers (100 or fewer employees) that establish pension plans. The credit would cover up to 50 percent of small-employer pension plan start-up costs, with a limit of \$1,000 for the first year and \$500 for each of the second and third years.

In addition, the bill would require small employers that offer a SIMPLE 401(k) plan to contribute at least 1 percent of eligible employees' compensation to their accounts, whether or not the workers make an elective deferral.

#### ***Small Business Pension Start-Up Credit Act of 1999***

H.R. 1021, co-sponsored by Reps. Debbie Stabenow (D-MI) and Dave Camp (R-MI), would create a tax credit for small employers (100 or fewer employees) that establish pension plans. The credit would cover up to 50 percent of small-employer pension plan start-up costs, with a limit of \$1,000 for the first year and \$500 for each of the second and third years.

#### ***Employee Pension Portability and Accountability Act of 1999***

H.R. 1213, sponsored by Rep. Richard Neal (D-MA), would provide a tax credit to small businesses establishing new retirement plans and allow small businesses to offer simplified defined benefit plans. The provisions are substantially the same as those contained in H.R. 1021, H.R. 1590, and S. 8 (see above).

# Appendix III

## SERS Fact Sheets and Small Biz Retirement Quiz

### *Small Employers Without Plans*

#### **Why Not?**

There are a number of reasons why most small employers do not offer retirement plans—it is not simply a matter of administrative cost and burden. For some, the main driver is the financial reality of running a small business, i.e., their revenue is too uncertain to commit to a plan. For others, the most important reasons for not sponsoring a plan are employee-related, e.g., it is not a priority for the employer's workers.

#### *Reasons Cited for Not Offering a Retirement Plan*

	Most Important		Major Reason	
	1998	1999	1998	1999
Revenue-Related Reason				
Revenue is too uncertain to commit to a plan	16%	19%	51%	50%
Employee-Related Reasons				
Large portion of employees are seasonal, part time, or high turnover	n/a	19	n/a	42
Employees prefer wages and/or other benefits	22	17	50	53
Cost and Administration-Related Reasons				
Costs too much to set up and administer	14	12	35	30
Required company contributions are too expensive	12	10	45	51
Too many government regulations	4	3	35	32
Other Reasons				
Vesting requirements cause too much to go to short-term workers	9	2	42	38
Don't know where to go for information on starting a plan	n/a	2	n/a	5
Benefits for the owner are too small	3	1	19	17

#### **Factors Leading to Serious Consideration of Offering a Retirement Plan**

The potential exists for increased plan sponsorship: 15 percent of small employers without a retirement plan reported that it is very likely their business will start one for their employees in the next two years, and 24 percent reported that it is somewhat likely.

Influencing Factors:	1998	1999
Increase in business profits	66%	69%
Business tax credit for starting a plan	64	67
Plan with reduced administrative requirements	50	55
Allowing key executives to save more in a plan	49	52
Demand from employees	49	46
Availability of easy-to-understand information	n/a	44
Lengthening of vesting requirements	n/a	33

#### **Company Demographics**

Differences exist when comparing plan sponsors and nonsponsors.

	Plan Sponsor	No Plan
Approximate Gross Revenue in Previous Year		
Less than \$2 million	34%	63%
\$2 million or more	48	18
Not reported	19	20
Age of Most Full-Time Employees		
Under age 30	11	23
Ages 30–39	62	51
Ages 40 and older	24	25
Annual Salary of Most Full-Time Employees		
Under \$20,000	9	32
\$20,000–\$40,000	73	58
Over \$40,000	11	8

Source: Employee Benefit Research Institute, American Savings Education Council, and Mathew Greenwald & Associates, 1999 Small Employer Retirement Survey.



## Small Employers With Plans

### **Type of Retirement Plan Offered**

			Company Size		Gross Revenue	
	1998	1999	5–20	21–100	< \$2 million	\$2 million +
Defined Contribution (DC) Plan Only	84%	84%	83%	85%	83%	86%
Defined Benefit (DB) Plan Only	7	2	1	3	3	1
Both DC & DB Plans	8	7	6	7	7	8

### **DC Plan Type Offered**

While no differences are found in the general type of retirement plan offered (i.e., DC, DB, or both), demographic differences among small employers are seen when examining the different types of defined contribution plans that are offered.

- 401(k) plans are more likely to be offered by companies with more than 20 employees and by companies with higher revenues.
- Both SIMPLE and SEP plans are more likely to be offered by companies with 5–20 employees.
- SIMPLE and 403(b) plans are more likely to be offered by companies with gross revenues of less than \$2 million.

### **Among Employers Offering a DC Plan—**

			Company Size		Gross Revenue	
	1998	1999	5–20	21–100	< \$2 million	\$2 million +
401(k) plan	61%	67%	51%	76%	51%	76%
Profit-sharing plan	31	26	25	26	24	30
SIMPLE plan	12	11	24	4	18	6
403(b) plan (educational/nonprofits)	8	10	9	10	15	6
Simplified employee pension (SEP)	9	8	15	5	13	6
Money purchase plan	4	4	4	3	1	5
Employee stock ownership plan (ESOP)	6	1	1	2	0	3
Thrift savings plan	4	1	0	2	1	1

### **Reasons for Offering a Plan**

Small employers offering a retirement plan cited several reasons for doing so. In many cases, there are direct business benefits to the employer from sponsoring a retirement plan.

	Most Important		Major Reason	
	1998	1999	1998	1999
Competitive advantage in employee recruitment/retention	24%	33%	56%	60%
Positive effect on employee attitude and performance	16	28	68	71
Employers have obligation to provide plan for employees	n/a	12	n/a	29
Tax advantages for employees	5	7	39	38
Tax advantages for key executives	8	6	29	25
Employees demand or expect it	4	5	25	21

Source: Employee Benefit Research Institute, American Savings Education Council, and Mathew Greenwald & Associates, 1999 Small Employer Retirement Survey.

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## Small Biz Retirement Quiz

Do you think you have a pretty good idea of what is involved in sponsoring a retirement plan? Do you think you have a good feel for how much it would cost to sponsor a 401(k) plan for your workers? Find out for sure. Take the *Small Biz Retirement Quiz*, and compare your knowledge with that of your peers.

### The Quiz

- |  |      |       |
|--|------|-------|
| 1. You legally must match everything an employee contributes to a 401(k) plan.   | True | False |
| 2. Once you set up a plan, you can never terminate it.   | True | False |
| 3. You can share the administrative costs of a plan with your employees.   | True | False |
| 4. A company that offers a retirement plan is legally required to offer the plan to all of its employees.  | True | False |
| 5. Generally, companies with 401(k) plans are legally liable for the investment choices employees make.  | True | False |
| 6. In a 401(k) plan, an employee is always automatically vested in (entitled to) any money contributed by the employer to his or her account.                          | True | False |
| 7. For \$2,500 per year, a small employer could cover the operation of a basic 401(k) plan, including the costs of record keeping, administration, and communications. | True | False |

### How well did you do?

Correct answers:

1. False—It is up to the plan sponsor whether or not to include a matching provision in the plan.
2. False—Establishing a plan does not commit you to it forever.
3. True—It is up to the plan sponsor whether or not plan expenses are shared with plan participants.
4. False—Subject to legal limits, not *all* employees must be covered by a plan if offered.
5. False—Companies are responsible for offering enough good investment *options*, but not for the *choices* that workers make (as long as the employer does not breach its fiduciary responsibilities).
6. False—The law allows a plan sponsor to vest participants in company contributions over time.
7. True—Many service providers offer basic plans for less than you might expect.

If you did not do too well, you have plenty of company. The *Small Biz Retirement Quiz* was included in the 1999 Small Employer Retirement Survey. Among a nationally representative sample of small employers without retirement plans, 19 percent answered six to seven questions correctly, 62 percent answered three to five questions correctly, and 19 percent answered zero to two correctly.

Question 1 was answered correctly by 57 percent of small employers without a plan. Question 2 was answered correctly by 87 percent. Question 3 by 57 percent, question 4 by 30 percent, question 5 by 68 percent, question 6 by 41 percent, and question 7 by 49 percent.

Small employers that sponsor plans did only slightly better.

Source: Employee Benefit Research Institute, American Savings Education Council, and Mathew Greenwald & Associates, 1999 Small Employer Retirement Survey.

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## Appendix IV

### Resources for Small Employers

America's 5.3 million small businesses (with 100 or fewer workers ) employ more than 38 percent of the private-sector work force in the United States. Following are several resources for small-business owners or those thinking about starting a business. Information is also available for small employers who are thinking about starting a retirement or pension plan for their employees.

The Department of Labor's **Pension and Welfare Benefits Administration** (PWBA) protects the integrity of pensions, health plans, and other employee benefits for more than 150 million people. The Department of Labor (DOL) launched a campaign in 1997 designed to educate small-business owners about various retirement plan options. Materials outlining these options are available on DOL's Web site, located at [www.dol.gov/dol/pwba](http://www.dol.gov/dol/pwba).

PWBA has also launched a new interactive Web site, "The Small-Business Retirement Savings Advisor," providing answers to questions about retirement savings options for small employers and allowing individuals to determine which program is most appropriate for a business.

The **National Federation of Independent Business** (NFIB) is the largest advocacy organization representing small and independent businesses in Washington, DC, and all 50 state capitals. A list of frequently asked questions and a page with small business bookmarks, including how to start a business, choosing a location, employees and benefits, and business trends, can be found on their Web site, located at [www.nfib.org](http://www.nfib.org).

The **U.S. Chamber of Commerce** is the world's largest business federation, representing nearly three million companies, 3,000 state and local chambers, 775 business associations, and 85 American Chambers of Commerce abroad. The Chamber's Web site is located at [www.uschamber.com/smallbiz](http://www.uschamber.com/smallbiz), where small employers can find online tools and resources for small businesses, as well as a retirement program for small employers.

The **U.S. Small Business Administration** (SBA), established in 1953, provides financial, technical, and management assistance to help Americans start, run, and grow their businesses. SBA is the nation's largest single financial backer of small businesses, and last year offered management and technical assistance to more than one million small-business owners. The SBA Web site is located at [www.sba.gov](http://www.sba.gov) and offers information on starting, financing, or expanding a small business.

Additionally, local small-business development centers can help current small business owners or individuals interested in starting a business.

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# Issue Brief

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