EBRI NOTES

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THE 1982 TAX BILL: ONLY A DARK CLOUD OR SOME SILVER LINING?

The sponsorship and servicing of employee benefit plans will change as a result of the new tax bill. And, the structure of the universe of pension plans will change as well.

The provisions contained in the new law will become the subject of evaluation. Policymakers will assess the possible need for corrective legislation. Provisions such as movement for some plans to 1.0, 3 year cliff vesting, 6 year graded vesting or the provision of a minimum benefit will also be evaluated in terms of the consequences of having them extended to all pension plans.

As important, those proposals discussed until the moment of final House/Senate compromise should be examined carefully. For example, the proposed extension of full nondiscrimination rules to all welfare plans. Or, the full elimination of the COLA on maximum benefit and contribution limits. Or, placing an absolute cap on federal retiree COLAs. The new law did take first steps by placing nondiscrimination requirements on group term life insurance and limiting the amount of federal retiree COLAs for those under age sixty-two. What are the implications for the future of employer-provided benefits and Social Security?

Another question is worth contemplation. Could the new tax law take "reform" pressure off the employee benefit system? The perceived "abuse" situations that will "remain" with these new rules will be "fewer." The ability in the future to receive the type of press generated by Rangel and Dole, "only the rich will suffer," has been greatly reduced. Further, the new law may make meaningful "reform" of Social Security to assure its financial future more likely.

Interestingly, the employee benefits community was better prepared to deal with Congress on this bill than ever before. Without question, the result could have been "far worse." Encouragingly, the community finds itself in a position unique to its history -- the vehicles exist to do the evaluation that is needed and to inform policymakers of the results. Only the resources may be somewhat scarce. This is clearly different than during the "dog days" of ERISA when both the vehicles and the resources were scarce. The thirst for this newly available data was shown by the Washington Post when it used EBRI Issue Brief #10 as the basis of an editorial on August 13, 1982 (reproduced on p.2).

The continuing government focus on bringing revenue and expenditures into line will place additional cost and performance pressures on the employee benefits community -- public and private. Private pension benefit changes in the tax law will produce three-year revenue gains of approximately $2 billion; and public pension benefit changes will produce gains of nearly $5 billion. The necessity of documenting the accomplishments of employee benefits provision is all the more important in a cost-conscious environment. The long-term value of identifying potential "weaknesses" that may be targeted for legislative reform in the future cannot be overstated. The 1982 Tax Bill serves to remind us that the "time to anticipate and plan is now." D.L.S.

FRIDAY, AUGUST 13, 1982

The Washington Post

AN INDEPENDENT NEWSPAPER

A Lid on Government Pensions

SHOULD FEDERAL pensioners share in the burden of controlling the federal budget? That's an issue that Congress would like to sidestep in this election year, although the budget resolution adopted by both houses called for curtailing increases in both civilian and military pensions.

The Senate has voted by a slim margin to cap cost-of-living adjustments for federal retirees at 4 percent a year for the next three years, thereby saving $5 billion. The House, however, has rejected such a cap by a substantial majority. A House-Senate conference is trying today to resolve this considerable difference.

Congressional reluctance to limit federal pensions arises not only from due regard for the powerful civil service lobbies but from a feeling that it's not fair to take something away from federal pensioners and not from other retirees as well. Although many federal retirees also draw indexed Social Security benefits, some do not, and retirees from low-paying federal jobs may have only modest pensions.

That's all true, but it doesn't address the fact that all over the country people are enduring much harsher losses than a temporary limit on benefit increases. Jobs are being lost, welfare benefits are being cut and firms are going bankrupt. Moreover, few private sector pensioners have had the full—excessive, really—protection against inflation that federal retirees have enjoyed.

The fact is that both federal civilian and military pensions are considerably richer on average than other pensions. The Employee Benefit Research Institute calculates that federal pensions are almost three times larger than average private sector pension payments—although Social Security payments narrow this difference somewhat. It is true that the better private pensions provide comparably generous benefits, but virtually none provides the full indexation of benefits and early retirement provisions that are part of federal pensions. Moreover, because of early retirement provisions, the majority of federal retirees now hold other jobs.

As a result of this generosity, spending on civil service and military pensions will exceed $37 billion next year. Although federal employees contribute 7 percent of their salaries to the retirement fund, the actual cost of their pensions is more than five times that amount. The rest must be paid for by taxes on the income of other people—most of whom aren't getting any inflation protection at all.

The government needs to have adequate pension plans in order to recruit and retain high-quality military and civilian personnel. But the cost of currently promised benefits has already become a significant burden on taxpayers and an even larger claim on the resources of future generations. Federal pensions need a more thorough review than the budget process can provide, but for the moment it is not too much to ask that the current beneficiaries of those pensions make a small contribution to efforts to control federal spending.

THE WORLDWIDE CRISIS IN SOCIAL SECURITY: THE UNITED STATES IS NOT ALONE AND IT IS BETTER OFF THAN MANY OTHER NATIONS

All nations are facing an unavoidable need to reduce the generosity of their Social Security systems while simultaneously increasing taxes to support these programs. This was the principal conclusion reached at a recent internationally attended seminar on retirement income held in Salzburg, Austria.[1/]

The Salzburg session was attended by government policymakers, corporate benefit specialists and academics representing twenty developed and developing nations. While there was a consensus that these problems could be solved, the political environment will make this difficult. The following points of consensus were agreed upon:

- Changes are likely to be at the margin of programs rather than wholesale restructuring.

- Significant benefit retrenchments will be necessary most immediately in Europe and elsewhere later on.

- Increased attention must be paid to private provisions and to the careful coordination of all sources of retirement well-being (i.e., cash income, assets or in-kind benefits).

- The likelihood of needs-based minimum income programs being developed will increase the longer changes in Social Security are delayed.

Both the seminar and the Institute for Contemporary Studies publication (see footnote 1) served to highlight contradictions similar to those that characterize the debate in this country. The following list includes examples of these opposing points of view:

concern over financing and adverse effects on economic growth	vs.	desire for 70 percent income replacement and fully indexed benefits
desire for maximum employment flexibility to enhance productivity	vs.	discussion of mandating employer pensions
desire to focus on retirement income provision	vs.	use of the programs to get people to retire early
desire for total benefit security	vs.	desire to use pension assets for a "new economics" and for social expenditures

[1/] The same conclusion has been reached in a recent publication by the Institute for Contemporary Studies entitled The World Crisis in Social Security, edited by M. Jean-Jacques Rosa. For more information contact: Pamela Riley, Institute for Contemporary Studies, Suite 811, 260 California Street, San Francisco, CA 94111 (415) 398-3010.

concern for retirement income adequacy	vs.	desire for lump-sum distributions
desire for earnings-related benefits	vs.	a minimum income on a universal basis

A discussion of these apparent contradictions served to highlight major differences between the United States and other countries -- differences which are central to policy decisions. Other countries have more workers than they need and are considering reductions in retirement ages in order to open up more jobs. The United States, however, is entering a period in which it is expected that we will want to encourage longer periods of labor force participation. This one difference makes the needs and possible solutions for the United States very different from most other nations.

During the concluding seminar session, there was a consensus that generalization was possible only to the extent that every country has a major problem. Beyond such a conclusion, the social and economic dynamics of each nation make it nearly impossible to transfer solutions.

Papers from the Salzburg seminar will be available later this year. The paper by Dallas Salisbury, "The Private Pension System in the United States," will be published in Benefits International (September Issue) and a summary of the full seminar by the International Benefits Information Service.

NEW RESEARCH FINDINGS

Funding Status of Federal Pension Plans

Public Law 95-595, passed in 1978, requires all federal pension plans to submit an annual report to Congress on their financial and actuarial status. All annual reports must utilize consistent actuarial and economic assumptions. Reports must include: (1) calculations of financial position; (2) present value of accumulated benefits; (3) accrued liability; and (4) the normal cost of the plan. Projected flows of plan disbursements also must be included in the report.

Table 1 illustrates the change in unfunded liabilities among the largest federal pension programs for the years 1979-1980. Total unfunded liabilities grew over $145 billion (17.2 percent) at the end of 1980. In 1980, the total unfunded liabilities for all four plans was $996.38 billion. Total assets were $74.31 billion.[1] The Civil Service and Military Retirement Systems accounted for most of the growth. The Civil Service Retirement System had 2,700,000 active participants and 1,772,000 beneficiaries; and the Military Retirement System had 2,887,000 active participants and 1,333,000 beneficiaries in 1980.

[1] Public Law 95-595 reports filed with the U.S. Congress.

TABLE 1

Unfunded Liabilities of Federal Pension Programs — 1979-1980

Plan	1979 Unfunded Liability	1980 Unfunded Liability	Net Change in Unfunded Liability	
	(billions)	(billions)	(billions)	(percent)
Civil Service Retirement	$403.10	$469.50	$66.40	16.5%
Military Retirement	444.60	523.30	78.70	17.7
Department of Defense (nonappropriated funds)	.49	.58	.09	18.4
Foreign Service Retirement	2.30	3.00	.70	30.4
TOTAL	$850.49	$996.38	$145.89	17.2%

Source: Public Law 95-595 reports filed with U.S. Congress.

1 This plan covers civilian personnel employed at military exchanges.

NEW FOUNDATION TO ADDRESS PROBLEMS OF THE ELDERLY

Philippe Villers, a Boston entrepreneur, intends to establish a new foundation to deal exclusively with the problems of aging and the elderly. According to a Washington Post article on August 10, 1982, the purpose of the foundation--described in a prospectus--is to reshape public attitudes and policies which concern the elderly. The Villers Foundation, with assets of $40 million, will be among the largest 5 percent of the 22,500 foundations in the United States. The article also noted that the Retirement Research Foundation in Park Ridge, Illinois is the only foundation which deals exclusively with problems of the elderly.

DEPARTING DIRECTOR OF THE NATIONAL INSTITUTE ON AGING CALLS FOR MANDATORY PRIVATE PENSIONS AND NEW GOVERNMENT COORDINATING BODY

Robert N. Butler, soon to become Chair of the Geriatrics Department at New York's Mount Sinai Medical Center, made these recommendations in an interview published on July 31, 1982 in the National Journal. Butler argued that the government is "waiting until the crisis happens" by failing to establish a consistent federal policy that addresses the needs of the elderly (today and in the future).

For more information see: Linda E. Demkovich, "Still No Federal Policy on Aging, Warns Aging Institute's Director," National Journal, July 31, 1982, pp. 1344-1346.

EBRI ACTIVITIES

EBRI 1982 Annual Meeting — October 20-21, 1982

EBRI's 1982 Annual Meeting will feature a policy forum on October 20 entitled "Public Policy, Pension Liabilities and Financial Markets: Issues, Effects and Options." The forum will be moderated by Dave Williams, Alliance Capital Management Corporation. Papers are being prepared by: Edward Boynton, The Wyatt Company; Harold Dankner, Coopers & Lybrand; Douglas Love, Buck Consultants, Inc.; Patrick Regan, BEA Associates; and Jack Treynor, Treynor-Arbit Associates. Proposals are now being considered by Congress which would increase pension plan sponsor liabilities to the Pension Benefit Guaranty Corporation. Further, the Financial Accounting Standards Board is considering the issuance of guidelines which would require the placement of assets and liabilities on the corporate balance sheet. These important proposals will be discussed in-depth at the October forum.

Members and Associates will join the Board of Trustees on October 21 to review EBRI's past activities and to establish an agenda for 1983.

EBRI Research Director Participates in Conference

Sylvester J. Schieber, EBRI Research Director, presented a paper on July 16, 1982 at the Western Economic Association meeting in Los Angeles, California. The paper, "The Evolving Role of Private Retirement and Savings Programs and Public Welfare Programs in the U.S. Retirement System," focuses on the elderly's major income sources other than Social Security. It discusses the historical role that various income sources have played in providing income security for the elderly and looks at their potential future role. The paper will be published in Economic Inquiry later this year.

For more information contact: Sylvester Schieber, EBRI, 1920 N Street, NW, Suite 520, Washington, DC 20036 (202) 463-8148.

Recent EBRI Publications

Issue Briefs

"State and Local Government Pension Plans: Is Federal Regulation Coming?" Issue Brief #11, August 1982.

"Federal Pensions: An Island of Privilege in a Sea of Budget Austerity," Issue Brief #10, July 1982.

"Prospective Hospital Reimbursement: For What, For Whom?" Issue Brief #9, June 1982.

"The Pension Equity Tax Act," Issue Brief #8, June 1982.

Issue Briefs are available for $2.00 each (prepaid).

An Upcoming EBRI Publication

Economic Survival in Retirement: Which Pension Is for You?

The EBRI Education and Research Fund sponsored a policy forum on May 20, 1982, entitled, "Defined Benefit/Defined Contribution Plans: Understanding the Differences." Speakers and discussants examined the significance of apparent shifts in defined benefit and defined contribution plan growth and individual versus employer provisions. The following questions were addressed: (1) What are the advantages and disadvantages of defined benefit and defined contribution plans for employers? employees? (2) Which approach offers employees the most secure retirement income promise? (3) Should the government encourage creation of defined contribution plans or defined benefit plans? (4) Should the government favor either employer-sponsored or individual provision? (5) Should the government take a neutral position on these issues? Selected speaker presentations and the edited forum discussion will be compiled in this book to be published in September - $10.00. For a summary of the forum's discussion see EBRI Notes, May/June issue.

ALL PUBLICATIONS ARE AVAILABLE THROUGH EBRI, 1920 N STREET, NW, SUITE 520, WASHINGTON, DC 20036 (202) 659-0670.

OUTSIDE PUBLICATIONS

Limited Period Early Retirement Incentive Programs
By Towers, Perrin, Forster & Crosby

Many companies, trying to avoid the need for layoffs in today's slow economy, are accelerating their normal rate of employee attrition through special incentives for early retirement. This recent study discusses the design and communications issues that must be considered before adopting an early retirement incentive program. Often, a company's regular early retirement benefits do not make retirement attractive or affordable. These incentive programs can: (1) "assist in streamlining organizational structure"; (2) "provide a means of terminating less productive employees"; and (3) "help open more attractive career paths for the firm's younger employees." The study analyzes ten major companies' early retirement incentive programs and finds that in six of these companies, more than half of the eligible employees "took advantage of the inducement to retire early." Critical issues to consider in designing a limited period early retirement plan are the incentive factor and the duration of the offer.

For more information contact: Edward L. Hansen, Towers, Perrin, Forster & Crosby, 600 Third Avenue, New York, NY 10016 (212) 661-5080.

Child Care Assistance: Issues for Employer Consideration
By Hewitt Associates

Relatively few employers have provided child-care assistance to employees. Reasons for employer's hesitance have included: (1) cost factors; (2) concern about the acceptance among other employees not in need of this benefit; (3) reluctance to intrude in what might be considered a private family matter; and (4) unfavorable tax laws. (Employer payments for child care previously constituted taxable income to the employee.) Under the 1981 Economic Recovery Tax Act, payments for child care are no longer taxable income to employees provided certain conditions are met. Removal of tax barriers has prompted some employers to look into child-care assistance programs. This background paper focuses on the available options and considerations for employers who may wish to provide such assistance. Included is a summary of child-care programs currently in operation.

For more information contact: Hewitt Associates, 100 Half Day Road, Lincolnshire, IL 60015 (312) 295-5000.

<u>An Analysis of the Costs of Pension Accrual After Age 65</u>
Prepared by Anna M. Rappaport for the Select Committee on Aging, House of Representatives

This report explores the cost implications of defined benefit pension accruals for individuals who work past the age of sixty-five. Two questions are examined: (1) "Will a delay in retirement age beyond normal retirement cost the plan more or less than a retirement at normal age retirement?" (2) "Will plan costs as a percentage of payroll increase because of delayed retirements?" The overall findings suggest that "for most defined benefit plans there is no actuarial or cost reason to justify freezing pension accruals at the normal retirement age of sixty-five." Also, there is no support for the argument that pension accruals for work after the age of sixty-five would cost companies more than pension accruals for workers between the ages of sixty and sixty-four.

For more information contact: House Select Committee on Aging, 712 House Office Building, Annex 1, Washington, DC 20515 (202) 226-3375.

<u>Unemployment, Unsatisfied Demand for Labor, and Compensation Growth in the United States, 1956-1980</u>
By James L. Medoff and Katharine G. Abraham

This study assesses the value of unemployment rates as barometers of labor market tightness. The findings indicate that: "Labor market pressure on wages can be more reliably assessed by looking at measures of unsatisfied labor demand than by looking at the unemployment rates on which most earlier analyses have focused." The authors present two arguments to support their findings: (1) "While both unemployment rates and unsatisfied labor demand proxies perform reasonably well on their own in compensation growth equations, in models which include both, only the unsatisfied demand variable appears to matter." (2) "The past decade's outward shifts in Phillips plots can to a substantial degree be tied to outward shifts in plots pairing the relevant unemployment rate and unsatisfied demand proxies."

For more information contact: James L. Medoff, Department of Economics, Harvard University, Littauer Center 115, Cambridge, MA 02138 (617) 495-4209 or Katharine G. Abraham, Sloan School of Management, Massachusetts Institute of Technology, E52-445, Cambridge, MA 02139 (617) 495-4209.

The 1982-83 Chartbook of Federal Programs in Aging
By Irma Schechter and William Oriol

The 1982-83 Chartbook serves as a reference guide in obtaining information on federal funding in the aging field. The publication includes: (1) a section on new block grants; (2) charts covering 132 major federal programs on aging research, training and services; (3) "perspective notes" to clarify how a program relates to the aging field; and (4) appendices providing contacts (i.e., congressional and federal agency offices, clearinghouses and libraries).

For more information contact: Care Reports, Inc., 4715 Cordell Avenue, Bethesda, MD 20814 (301) 986-1607.

"General Revenue Financing of Medicare: Who Will Bear the Burden?"
By Janet L. Johnson and Stephen H. Long

Recently, two national advisory committees on Social Security have recommended major shifts in Medicare financing in order to preserve the financial viability of the Social Security trust funds. Johnson and Long, using a microsimulation model, estimate the income redistribution consequences of these two proposals in contrast to current law. The estimates show that the new proposals would substantially increase the progressivity of Medicare financing across household income levels. The first proposal would finance 50 percent of Medicare Hospital Insurance from general revenues; while the second proposal would finance 100 percent from general revenues. (Currently Hospital Insurance--Medicare Part A -- is financed from Social Security payroll tax; Supplemental Medical Insurance--Medicare Part B--is financed by enrollees' premium payments and a general revenue subsidy.) Neither proposal would affect the financing of Medicare Supplemental Medical Insurance. The estimates suggest that present financing is placing surprisingly large burdens on elderly families and that this burden would increase with these proposals.

For more information see: Janet L. Johnson and Stephen H. Long, "General Revenue Financing of Medicare: Who Will Bear the Burden?" Health Care Financing Review, March 1982, pp. 13-20.

The Employee Benefit Research Institute (EBRI) was established in 1978 to contribute to the development of public policy in the employee benefit field. EBRI, a nonprofit organization, has a broad membership that includes private sector companies and individuals with interests in employee benefit education, research and public policy.

EBRI also has a separate Education and Research Fund (ERF) which is operated exclusively to conduct charitable educational and research activities. The Fund is tax exempt under section 501(c) (3) of the Internal Revenue Code and is not a private foundation. EBRI Associates make contributions or grants to the Fund which are deductible as charitable contributions.

EBRI's policy forums, research studies, issue briefs, pamphlets and other publications aid public and private sector decision makers, managers, the press and the general public in formulating and articulating positions on employee benefit issues. As health and retirement issues receive increasing attention, the Institute strives to make effective and responsible contributions to public policy.

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EBRI NOTES, a bimonthly newsletter, includes information about: 1) newly released employee benefit statistics; 2) brief summaries of EBRI's ongoing research studies and forum discussions; and 3) reviews of outside research and publications.

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