Statement of
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Subcommittee On Labor
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On S. 1541

Any opinions stated in this testimony are Mr. Salisbury's.
INTRODUCTION

Providing for retirement income in the United States has taken on economic dimensions foreseen by very few as recently as 1974. The long-term costs of meeting retirement income promises already made is staggering:

- several trillion dollars for Social Security;
- nearly one-trillion dollars for federal employees;
- billions for state and local employees;
- billions for private-sector employees;

Meeting these costs could prove to be the major policy issue in the retirement income area in the decade ahead. How it is answered will be of tremendous importance to all those involved – which means every American.

For example, were the decision made to expand benefit provisions through Social Security and to raise payroll taxes to a level sufficient to meet all Social Security obligations, the demand for private plans and the dollars available to fund private plans would decrease.

In addition, extant research indicates that Social Security contributions at best have no effect on aggregate savings levels while private pension contributions increase aggregate savings by between 35¢ and 80¢ per contributed dollar. Clearly indicating that a shift from private pensions to Social Security could have a negative effect on savings and capital markets.
ERISA AND PRIVATE PENSIONS

The Employee Retirement Income Security Act of 1974 (ERISA) has a formative history that goes back at least to 1955. While the reaction to jobs lost through the closing of the U.S. Studebaker auto plant was one of regret, reaction to the fact that some accrued pension benefits would not be paid was met with shock and anger. With the Studebaker closing, the movement for "reform" began in earnest, culminating in the passage of ERISA.

COVERAGE AND PARTICIPATION

ERISA established age 25, one year of service and 1,000 hours of work as the required minimum standard for pension plan participation. Adjusting for agricultural and self-employed persons this "ERISA" workforce represents 49.7 million workers, out of a total workforce of 95.4 million. Employer plans cover 74% of the ERISA workforce: 68.3% actively participate. Of participants who had 10 or more years of service in current jobs, 78% were vested and another 11.4% did not know their vesting status.

Mature industries have even higher levels of coverage. In 1979 relevant workforce coverage in the Mining industry was 88.8%, in Manufacturing 81.9%, and in Transportation 79.9%. If only private establishments with 1,000 or more employees are considered, in 1979 the coverage rate was 95.8%.

And, contrary to reports, private pension plan growth has not stopped. In 1950 9.8 million participated in plans, by 1979, 35.2 million participated: participation growth of 263%, compared to labor force growth of 89% During 1980 new plan qualifications included 3.8 million partici-
pants and from January 1, 1981 to June 30, 1981 an additional 2.3 million participants.

In spite of adverse experience immediately following passage of ERISA, net plan formation since 1974 totaled 197,523 plans. In 1976 there were only 3,494 net new plans; in 1980, 56,063. During the first half of 1981, 31,478 new plans were formed.

Those not covered by a private plan can be clearly identified:

- 31% of workers report that they are working for firms with less than 100 workers, yet they represent 67.1% of the noncovered;

- Trade and Service employees generate 38.7% of jobs, they represent 58.4% of the noncovered;

- 27.7% have annual earnings below $10,000, they represent 44.1% of the noncovered;

- 42.3% have been with their current employer for five years or less, but constitute 57.9% of the noncovered.

The noncovered work in newer industries, for small employers, for shorter time periods and at relatively low wages.

The noncovered represent 23% of the ERISA workforce. Present policies plus individual provisions will provide retirement income to many of these persons by the time they reach age 65. Research undertaken in 1980 by the President's Commission on Pension Policy and reformulated in 1981 for EBRI indicates that 70% to 80% of those reaching 65 at the turn of the century will receive private pension income. For others, particularly those with limited workforce attachment, government transfer programs may be the only effective means of providing "retirement" income.
ASSETS

Pension funds held assets of $687 billion at the end of the second quarter of 1981, ($478.4 billion private; $208.6 billion state and local). These funds grew from 5% to 16% of total financial assets from 1950 to 1980. In 1979, the top 25 corporate funds held $120 billion; the top 25 public funds held $126-130 billion; the top 25 Taft-Hartley funds held $12 billion. Private assets grew 35-fold from 1950 to 1980 (13.25% per year), state and local assets grew 40-fold (13.8% per year) with a net inflow for private funds in 1980 of $22.3 billion.

The U.S. Department of Labor and the U.S. General Accounting Office have both made estimates of future asset levels - assuming no changes in public policy. These forecasts project total assets of $3 trillion in private plans and $975 billion in state and local plans by the mid-1990's.

Major public policy changes may well be made in the Social Security program which could have a dramatic effect on these future asset projections.

INTERACTION WITH SOCIAL SECURITY

Any of the following changes in Social Security could have important consequences for private and public employer plan contribution levels, asset accumulations and individual initiatives:

- raising retirement ages
- reducing the level of indexing
- adjusting the benefit calculation formula
- speeding up increases in the payroll tax
- universal coverage
Public and private employer pensions and individual effort are playing an increasingly important role. The continued level of effort will be affected by future Social Security policy, future policy on in-kind benefit programs, and future federal regulatory policy. Given these facts the need for national attention to retirement income policy on a comprehensive basis cannot be stated too strongly.

**WHY ERISA?**

ERISA specified the following problems that required legislative solution (Act Section 2):

1. lack of employee information;

2. due to the lack of vesting provisions many employees with long years of employment were losing anticipated benefits;

3. due to the inadequacy of minimum funding standards, the soundness and stability of plans with respect to adequate funds to pay promised benefits might be endangered;

4. due to the termination of plans, employees have been deprived of anticipated benefits.

These problems led to articulation of specific policy:

1. Require reporting and disclosure ... establish fiduciary standards ... require vesting of accrued benefits of employees with significant periods of service ... establish minimum standards of funding ... and require plan termination insurance.

2. encourage the continuation and maintenance of voluntary private pension plans and the timely and uninterrupted payment of pension benefits.
The Act also allows for the undertaking of research and surveys to collect, compile, analyze and publish data, information, and statistics relating to employer benefit plans.

The Departments of Treasury and Labor and the Pension Benefit Guaranty Corporation have worked continuously since the passage of ERISA to responsibly meet their obligations.

While there are many who feel that revision and refinement of ERISA is both needed and justified, few if any deny that ERISA was needed or advocate its repeal.

POST-ERISA EXPERIENCE

Experience since September 2, 1974 has been documented and analyzed thoroughly enough to allow an assessment of ERISA provisions. In fact, in some cases that analysis has been so complete that it has already led to major post-ERISA legislative changes in the plan termination insurance program. While the "market place" appears to have adjusted to the presence of ERISA, there is substantial evidence indicating that there are many changes that could be made to reduce plan costs without reducing the protections and safeguards provided by ERISA.

Further, such reforms could be expected to accelerate the rate of new plan formation and growth of participation that has been experienced since 1977; could remove the conditions that have caused no new multi-employer plans to be created; and, could remove special pressures on defined benefit plans.

Table 1 provides detail on plan and participation growth since 1976.
### Table 1

**Plan Qualifications and Participants for Selected Years**

<table>
<thead>
<tr>
<th>YEAR</th>
<th>STOCK BONDS</th>
<th>MONEY PURCHASE</th>
<th>PROFIT SHARING</th>
<th>TRASCO/ESOP</th>
<th>TOTAL</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>PLANS</td>
<td>PARTICIPATION</td>
<td>PLANS</td>
<td>PARTICIPATION</td>
<td>PLANS</td>
</tr>
<tr>
<td>1976</td>
<td>Number 1/</td>
<td>758</td>
<td>275,803</td>
<td>6,206</td>
<td>42,082</td>
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<tr>
<td></td>
<td>Percent 1/</td>
<td>3.5</td>
<td>30.1</td>
<td>28.9</td>
<td>4.6</td>
</tr>
<tr>
<td>1977</td>
<td>Number 2/</td>
<td>856</td>
<td>1,436,358</td>
<td>10,111</td>
<td>133,068</td>
</tr>
<tr>
<td></td>
<td>Percent 2/</td>
<td>2.4</td>
<td>9.0</td>
<td>28.6</td>
<td>2.7</td>
</tr>
<tr>
<td>1978</td>
<td>Number 3/</td>
<td>850</td>
<td>1,255,173</td>
<td>21,821</td>
<td>202,906</td>
</tr>
<tr>
<td></td>
<td>Percent 3/</td>
<td>1.3</td>
<td>32.4</td>
<td>33.2</td>
<td>5.2</td>
</tr>
<tr>
<td>1979</td>
<td>Number 4/</td>
<td>574</td>
<td>362,263</td>
<td>15,909</td>
<td>146,159</td>
</tr>
<tr>
<td></td>
<td>Percent 4/</td>
<td>1.0</td>
<td>17.9</td>
<td>28.1</td>
<td>7.2</td>
</tr>
<tr>
<td>1980</td>
<td>Number 5/</td>
<td>182</td>
<td>1,043,653</td>
<td>19,706</td>
<td>193,133</td>
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<tr>
<td></td>
<td>Percent 5/</td>
<td>0.7</td>
<td>27.6</td>
<td>28.4</td>
<td>5.1</td>
</tr>
<tr>
<td>1/1 - 6/30</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1981</td>
<td>Number</td>
<td>190</td>
<td>180,400</td>
<td>7,802</td>
<td>155,955</td>
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<tr>
<td></td>
<td>Percent</td>
<td>0.6</td>
<td>7.9</td>
<td>24.8</td>
<td>6.8</td>
</tr>
</tbody>
</table>

*1/18 Plan Purchase Plans with 870 participants not shown separately.*

*2/6 Plan Purchase Plans with 454 participants not shown separately.*

*3/18 Plan Purchase Plans with 296 participants not shown separately.*

*4/4 Plan Purchase Plans with 120 participants not shown separately.*

*5/5 Plan Purchase Plans with 4 participants not shown separately.*

Source: EPRI Tabulations of IRS Data.
ADMINISTRATION

The TRIPARTITE agency administrative structure found in ERISA, based upon the legislative history, was quite clearly the result of political compromise. As a result of its initial inefficiencies the agencies agreed to a reallocation of responsibilities in 1976 and the Reorganization Plan Number 4 of 1979 made these adjustments permanent.

The review, conducted by the Office of Management and Budget in developing the Reorganization Plan, clearly indicated that substantial cost savings could be realized through consolidation into a single agency. The review also indicated that arguments for the current structure principally centered around the need to assure that multiple interests would be considered on major issues. The present structure, it is argued, provides that assurance.

IRAs AND DEDUCTIBLE CONTRIBUTIONS

The legislation (§ 1541) being discussed today highlights the importance of working towards a holistic national retirement income policy. Such a policy would generally be viewed as including an emphasis on individual effort in addition to government or employer sponsored programs.

Up through this year, 48 million persons were eligible for IRAs, with 5.3 million persons creating them. They are principally created by persons over age 25, working full time and earning more than $20,000. This group accounted for 4.4 million of all IRAs. Of the 5.8 million persons meeting these criteria and with more than one year of service, 75.9% created IRAs. With the extension of IRA eligibility to all workers, 25 of the 49 million new eligibles represent good IRA prospects in that they match the above criteria.

If 25% to 50% of these persons were to establish IRAs, the potential annual retirement income set aside could be as high as 20 billion dollars.
See Table 2.

IRAs have been criticized in the past for not providing for low income individuals. Available research indicates that this is true. IRAs generally provide for the moderate-income, full-time worker; they cannot be expected, based upon available information, to provide for low-income individuals. The government program safety net promises protection to low-income individuals with sporadic attachment to the workforce. IRAs will increase the number of persons with adequate income during retirement, but will not eliminate poverty among the elderly.

Corporate experience with thrift-savings plans and payroll deductions lends evidence that deductible employee contributions will be used. Many companies have achieved up to 80% utilization across all income groups. And, a recent survey indicated that over 50% of all workers will set aside additional dollars if given the ability to do so on a tax deferred basis.

These new approaches and opportunities can greatly enhance retirement income and move us towards more comprehensive ways of supplementing Social Security.

**REPORTING AND DISCLOSURE**

Reporting and disclosure requirements of ERISA have been among its most frequently criticized provisions. And, as a result, among the most analyzed.

A 1977 Department of Labor sponsored study indicated that small employer plan administrative costs were increased by as much as 100% by ERISA requirements.
<table>
<thead>
<tr>
<th>FACTOR</th>
<th>NUMBER ELIGIBLE</th>
<th>NUMBER IRAS</th>
<th>UTILIZATION</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(MILLIONS)</td>
<td>(MILLIONS)</td>
<td></td>
</tr>
<tr>
<td><strong>INCOME LEVEL</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>$&lt; 20,000</td>
<td>31.0</td>
<td>0.9</td>
<td>2.9%</td>
</tr>
<tr>
<td>$&gt; 20,000</td>
<td>18.0</td>
<td>4.4</td>
<td>24.4%</td>
</tr>
<tr>
<td>$20–$50,000</td>
<td>16.4</td>
<td>3.5</td>
<td>21.3%</td>
</tr>
<tr>
<td>$&gt; 50,000</td>
<td>1.6</td>
<td>0.8</td>
<td>50.0%</td>
</tr>
<tr>
<td><strong>AGE</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>25–64</td>
<td>25.0</td>
<td>5.3</td>
<td>21.2%</td>
</tr>
<tr>
<td>$&gt; 20,000</td>
<td>9.2</td>
<td>4.4</td>
<td>47.8%</td>
</tr>
<tr>
<td><strong>Service and Hours</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>25–64</td>
<td>15.0</td>
<td>5.3</td>
<td>35.3%</td>
</tr>
<tr>
<td>$&gt; 20,000</td>
<td>5.8</td>
<td>4.4</td>
<td>75.9%</td>
</tr>
</tbody>
</table>

Source: EBRI estimates from May 1979 CPS Data and Treasury Department Data, 1979.
A 1978 study conducted by Arthur Andersen & Company indicated that for a sample of 48 large employers the added administrative costs approximated 9 million dollars. Extrapolation indicates that for all plans the added costs could approximate 100 million dollars.

Three purposes were set forth in ERISA for the reporting and disclosure provisions:

1. to provide information to the government for purposes of enforcement;

2. to provide information for research studies called for in ERISA section 503; and

3. to provide information to plan participants and beneficiaries.

The common complaint in past hearings has been that no research has been presented to document or quantify the benefits achieved as a result of the above noted costs, or how effectively the noted purposes have been achieved. Our limited review indicates that:

1. Due to the agencies' enforcement focus on large plans and the lack of effectiveness with which the documents filed have been handled, there may be more information required than will be or can be effectively used.

2. Funding for finishing 1978 and 1979 statistical files was cut off in mid-1980 and the data will not be available for research studies. As a result, this reason for collecting certain information is removed. Many argue that if research is not to be done, the information now required to be filed might instead be required to be available upon demand.
3. There is no documented evidence showing that plan participants and beneficiaries make use of the information provided to them. Instead, there is a clear consensus that they discard the information in most cases. Again, many argue that access to much of the information on demand might meet the objectives of ERISA more efficiently.

To summarize, there is agreement that the purposes of ERISA are sound, but that the implementation might be made more efficient and effective.

**MINIMUM STANDARDS**

Research on the effects of the participation, vesting and funding provisions of ERISA has been quite extensive. Government and private-sector research indicates that:

1. The minimum standards set forth caused an increase in plan costs, a reallocation of plan benefits to shorter service workers, and a general strengthening of plan funding status.

2. Principal difficulties identified have been related more to the complexity of regulations than to requirements of the statute. For example, there are multiple definitions being promulgated for hour of service and year of service and IRS/Treasury initiatives regarding vesting (the 4/40 controversy).

3. Studies indicate that earlier participation or faster vesting would increase costs from 2% to 30% without any significant increase in benefits provided and an actual long term decrease in benefits provided to long-service workers.

To summarize, the statutory minimum standards of ERISA are generally viewed as both constructive and sufficient. There is, however, a documented concern over regulations that have been issued in the past.
FIDUCIARY STANDARDS AND PROHIBITED TRANSACTIONS

This area of ERISA represents one of the most important and controversial. For plan sponsors, concern has principally been over the time and expense that has been required to obtain exemptions from the agencies and the inability to continue what have been normal business practices that are viewed as legitimate. For fiduciaries, concern has principally been over the greater stringency of ERISA provisions as compared to the fiduciary requirements in other areas of activity. For investment specialists there has been concern that ERISA has discouraged venture capital investment. And, for a very diverse group there is a belief that these requirements have eliminated creativity in the investment of pension assets.

Research in this area has been limited. Articles, speeches and past testimony represent the only real resources. These resources:

1. highlight the fact that these provisions will become increasingly controversial as the size of pension assets continues to grow and multiple interests seek to move investments to their benefit;

2. provide example after example of transactions that require exemptions that the authors find it nearly impossible to view as abusive;

3. provide substantial evidence that the cases brought to date by the government would not have been harmed by less restrictive fiduciary and prohibited transactions provisions;

4. indicate that these provisions increase the cost of plans due to the necessity of constant legal review of even the smallest transaction by the plan and its fiduciaries.
To summarize, the fiduciary and prohibited transactions provisions of ERISA are shown by available information to have stopped certain bad practices while creating added plan costs and placing a special burden on many good practices. The same information indicates that there are ways to open up an easier path for the good without condoning the bad.

FUTURE PROSPECTS

Private sector reaction to the post-ERISA environment shows the tremendous resilience of our economic system. In spite of the new costs and administrative requirements of ERISA, private plan formation has nearly reached its pre-ERISA levels. New participation is growing rapidly, and there is every reason to believe that the market will respond to new incentives. In this case, a reduction in the costs of creating and maintaining a pension plan could provide such an incentive.

With the difficulties facing the Social Security system, the need for a complementary private employee benefit system has never been more clear.