Statement on

Retirement Income Policy

Before the

U.S. Senate Committee on Aging

Hearings on

"The Pension Gamble: Who Wins? Who Loses?"

June 14, 1985

of

Dallas L. Salisbury

President

Employee Benefit Research Institute

06/11/85

EBRI

T-43

Statement on

Retirement Income Policy

Before the

U.S. Senate Committee on Aging

Hearings on

"The Pension Gamble: Who Wins? Who Loses?"

June 14, 1985

of

Dallas L. Salisbury

President

Employee Benefit Research Institute

EMPLOYEE BENEFIT RESEARCH INSTITUTE

2121 K Street, NW Suite 860 Washington, DC 20037 Telephone (202) 659-0670

Mr. Chairman, I would like to begin by commending you and the other members of this Committee for scheduling this hearing on a subject of special importance to today's workers and retirees. The Employee Benefit Research Institute is a nonprofit, nonpartisan research organization based in Washington, DC. EBRI does not make recommendations for or against legislation the Congress may be considering, but we are pleased to make available to you and the Committee all the pertinent facts that may bear on your decisions.

In an April 1985 survey conducted by Hamilton and Staff, 58 percent of full-time workers rated the existence of a pension plan at work as being "very important." Only 15 percent of those polled felt that Social Security would be a major source of retirement income. Sixty-four percent believed they would have enough money in retirement, though most of these apparently believed that employer-sponsored pensions would enable them to achieve that goal. When asked if they would have enough to retire with a reduced pension, only 24 percent answered "yes." A full 82 percent of employees agreed with the statement that: "If employers did not provide benefits, the government would end up paying." The answers to these survey questions reflect the importance of employer-sponsored pensions to the American worker--and why this Committee is concerned about them.

The system of employer-sponsored pensions is becoming increasingly more important to the provision of retirement income nationwide. I choose the term "employer-sponsored" quite deliberately, because from a policy standpoint, the state and local government is an employer that provides benefits in much the same way as private-sector employers. Granted, the law with which you are concerned, the Employee Retirement Income Security Act, specifically does not cover anything but private-sector situations. But for virtually all of the issues about which you are concerned--coverage, vesting, portability, and adequacy of retirement income--the role of government employers should not, in my opinion, be left out of the analysis. This is particularly true since the tax treatment of these programs at the individual level is identical in both public and private settings.

The role of employers in providing pensions has increased dramatically, especially in the aftermath of World War II. Twenty-five thousand private employer-sponsored retirement income and capital accumulation programs existed in 1950 with accumulated assets of $12.7 billion. The participation rate for nonagricultural wage and salary workers was 25 percent.

Over 800,000 private employer-sponsored retirement and capital accumulation plans exist today with accumulated assets exceeding $925 billion. Were private pension plan assets to grow at the same rate as they have since 1968, which is highly questionable for a number of reasons, they would reach $7.5 trillion by the year 2000, according to some very rough estimates by EBRI. Today, there is an additional $300 billion in assets in state and local plans, which could grow to $2.7 trillion by the year 2000, again according to our very rough estimates. The coverage rate for private nonagricultural wage and salary workers is 50 percent (see Chart 1) and over 80 percent for public-sector employees.

In 1950, the percentage of retirees receiving pension income was negligible. By 1962, 16 percent of retired married couples and 5 percent of unmarried retirees received pension income. By 1982, a Census Bureau survey found 33 percent of over-age 65 married couples and 15 percent of unmarried retirees had private pension income. The Social Security Administration recently found that among new beneficiaries substantial numbers of retirees had pension income from an employer-sponsored plan: 56 percent of married couples had pension income--38 percent with private pension, 21 percent with public pension; and 42 percent of unmarried beneficiaries had pension income--27 percent with private pension and 16 percent with public pension.

For the "newly retired" couple in 1981, in cases where only the husband receives a benefit, the average Social Security check was $671 per month; those with pensions received an additional $656. When both the husband and the wife received benefits, the monthly Social Security check rose to $836 and the pension income rose to $899. The pension income was greater than the asset income, which added $539 per month.

As these statistics indicate, the retirement and capital accumulation plan system has grown significantly over the past 35 years in terms of participants, assets, benefit recipiency, and benefit amounts.

<u>How is the system changing?</u>

The absolute number of workers covered by pensions has continued to grow, but due to the large number of new jobs being created by small businesses, the percentage of the total work force covered by plans has declined. The primary reason: small business does not provide pension coverage at the high rate found in large businesses (see Chart 2). If this does not change, then pension coverage is nearly as high as it can ever be expected to climb. The United Kingdom, for example, has had 50 percent of the work force covered by employer pension plans for twenty years.

It is difficult to increase coverage and participation. Last year, for example, Congress enacted the Retirement Equity Act (REA), which reduced the age for participation from 25 to 21, and the age for counting service for vesting from 22 to 18. EBRI estimates that these changes increased participation by 530,000 workers--or about 1 percent--and increased vesting by 300,000--or about 1 percent. In short, only 5.6 percent of the 9.5 million workers between the ages of 21 and 25 worked for employers with plans <u>and</u> worked at least 1,000 hours per year <u>and</u> had been on the job for one year. The improvements from REA are real, but such minimum standard changes are no replacement for increases in coverage through new plan creation among small businesses.

<u>Who is covered?</u>

Forty-nine million of 88 million nonagricultural wage and salary workers were covered by employer-sponsored programs in May of 1983 (56 percent). Most covered workers earn relatively modest salaries. Over 76 percent of all covered employees and 70 percent of all vested employees earned less than $25,000 a year in 1983 (see Table 1).

When one considers those that ERISA required to be included in employer plans--i.e., those between the ages of 25 and 64 working 1,000 hours per year and on the job at least one year--the base drops to 54 million workers, of

What issues would portability raise for adequacy of retirement income?

A number of questions arise in the consideration of portability. First, would mandatory portability increase or decrease actual retirement income? As noted, if "portability" is defined as permitting cash outs which can be immediately spent, then it would decrease retirement income. If "portability" allows the individual to take cash out from a defined benefit plan and invest the funds, later realizing poor investment returns, the same may be true. On the other hand, higher investment returns would increase retirement income. But in that case you're betting that the average individual will be able to outperform the experienced money managers retained by pension plans.

Second, would portability discourage plan sponsorship? Probably not, if it simply took the form of requiring cash distributions. If, on the other hand, it involved creating a new portability agency to be financed by plan sponsors, it might discourage pension plans, particularly among small employers.

Third, would portability increase or decrease system costs? If employees simply paid cash or were required to roll over cash distributions to an existing financial intermediary, total system costs could remain relatively stable and simplification would be achieved. If a new agency were formed, as some have proposed, and employers have to transfer values in and out of defined benefit plans, experience indicates that cost and complexity would rise significantly.

Benefit Delivery

Congress must eventually decide what it is seeking to achieve with tax incentives and ERISA. Is the intent solely to provide retirement income, or is an equal objective savings and capital formation through deferral of income by employees for periods extending to the termination of covered employment or beyond? Program coverage may not be as important in both cases. The percentage of retirees with monthly pension income is only relevant to judging the retirement incentive, not the savings incentive, which can be served by distribution prior to retirement. Debates of the recent past have assumed that retirement income is the primary objective. Thus, the "Retirement Equity Act." Yet, with earlier participation, vesting, and a higher cash out limit, retirement income might actually be reduced as cash preretirement distributions increase. For savings plans, is it equitable that an individual can quit and take the money, while an ongoing employee can't have access to the funds in an emergency? Does equity dictate that even in a savings plan all the money that goes in stays in until some common point in time? These are not simple questions, but they need to be answered before more changes in the law are made that further confuse objectives. As noted, over time, the Retirement Equity Act will lead to millions of additional small cash distributions that will be spent. Is that what Congress actually wanted to do? Is that "Retirement Equity?"

Conclusion

Congress has provided incentives for retirement and capital accumulation programs for over 60 years. The incentives have worked well in both areas. Congress should not overlook the long history of incentives for income deferral and begin judging all programs against a retirement income standard unless Congress makes it clear that is where the priority lies. That may be the best national policy, but it should be recognized as the clear shift in policy that it represents. And policy changes intended to create retirement income should be carefully tested to assure that they meet that objective.

A national policy that redefines itself to be a national retirement income policy, rather than a retirement and savings policy, would demand many changes in the rules. But, the first question is whether this fundamental change is merited and desired.

-end-

TABLE 1: EMPLOYMENT, COVERAGE AND VESTING: DISTRIBUTION BY EARNINGS FOR NONAGRICULTURAL WAGE AND SALARY WORKERS, MAY 1983

EARNINGS	Number of Workers (000's)		
	Employment	Coverage	Total Vested Benefits
Total	88,214	49,530	28,708
$1-4,999	10,014	2,433	358
$5,000-9,999	15,323	5,747	2,023
$10,000-14,999	17,827	10,328	5,484
$15,000-19,999	13,101	9,422	5,874
$20,000-24,999	10,283	8,159	5,641
$25,000-29,999	5,515	4,365	3,048
$30,000-50,000	6,611	5,547	4,071
$50,000 and over	1,615	1,371	1,106
Not reported	7,924	2,158	1,105
	Percentage Distribution Within Earnings Group		
	Employment	% Covered to Employed	% Vested to Employed
Total	100.00%	56.15%	32.52%
$1-4,999	100.00	24.29	3.57
$5,000-9,999	100.00	37.51	13.20
$10,000-14,999	100.00	57.93	30.76
$15,000-19,999	100.00	71.92	44.83
$20,000-24,999	100.00	79.34	54.85
$25,000-29,999	100.00	79.14	55.26
$30,000-50,000	100.00	83.91	61.57
$50,000 and over	100.00	84.90	68.50
Not reported	100.00	27.23	13.94
	Percentage Distribution Across Earnings Groups[a]		
	% Employment	% of Coverage	% of Total Vesting
Total	100.00%	100.00%	100.00%
$1-4,999	12.47	5.14	1.30
$5,000-9,999	19.08	12.13	7.33
$10,000-14,999	22.20	21.80	19.87
$15,000-19,999	16.32	19.89	21.28
$20,000-24,999	12.81	17.22	20.43
$25,000-29,999	6.87	9.21	11.04
$30,000-50,000	8.23	11.71	14.75
$50,000 and over	2.01	2.89	4.01

SOURCE: Preliminary Employee Benefit Research Institute tabulations of the May 1983 EBRI/HHS CPS pension supplement.

[a] Percentages exclude 9.0% of employees whose earnings are not reported.

TABLE 2: EMPLOYMENT, COVERAGE AND FUTURE BENEFIT ENTITLEMENT BEFORE AND AFTER THE RECESSION, MAY 1983 AND MAY 1979

	Employment (000's and % of Employed)	Coverage (000's and % of Employed)	Future Benefit Entitlement (000's and % of Employed)
1983			
Civilian Employment (All employees & self-employed)	98,964 100.00%	51,530 52.07%	24,095 24.35%
Nonagricultural Wage and Salary Workers	88,214 100.00%	49,530 56.15%	22,217 25.19%
Nonagricultural Wage and Salary Workers age 25 to 64 only	68,252 100.00%	42,463 62.21%	20,934 30.67%
Nonagricultural Wage and Salary Workers age 25 to 64, working 1000 hours or more	61,586 100.00%	40,702 66.09%	20,476 33.25%
ERISA Work Force (age 25 to 64, working 1000 hours or more, one year of tenure or more)	54,363 100.00%	38,057 70.01%	20,027 36.84%
1979			
Civilian Employment (All employees & self-employed)	95,372 100.00%	53,445 56.04%	22,633 23.73%
Nonagricultural Wage and Salary Workers	85,181 100.00%	52,019 61.07%	21,399 25.12%
Nonagricultural Wage and Salary Workers age 25 to 64 only	63,201 100.00%	42,576 67.37%	19,836 31.39%
Nonagricultural Wage and Salary Workers age 25 to 64, working 1000 hours or more	58,009 100.00%	40,830 70.39%	19,522 33.65%
ERISA Work Force (age 25 to 64, working 1000 hours or more, one year of tenure or more)	49,736 100.00%	36,890 74.17%	18,941 38.08%

SOURCE: Preliminary Employee Benefit Research Institute tabulations of the May 1983 EBRI/HHS CPS pension supplement and May 1979 DOL/SSA CPS pension supplement.

TABLE 3

THE DISTRIBUTION OF COVERED AND NONCOVERED WORKERS
IN THE "NEAR-ERISA" WORKFORCE
AGES 25 THROUGH 64 WORKING 1000 HOURS OR MORE
BY SELECTED CHARACTERISTICS, MAY 1983

	Covered Workers (000's)	Distribution Across Groups	Workers Not Covered[a] (000's)	Distribution Across Groups
FIRM SIZE[b]				
Less than 100 employees	6,215	17.4%	12,352	68.1%
100 to 499 employees	5,545	15.6	2,465	13.6
500 or more employees	23,869	67.0	3,314	18.3
Total	40,702	100.0	20,894	100.0
UNION STATUS				
Union	15,223	38.2	2,163	10.6
Nonunion	24,627	61.8	18,155	89.4
Total	40,702	100.0	20,894	100.0
EARNINGS[d]				
Less than $10,000	4,107	10.4	6,711	34.6
$10,000 to $24,999	24,545	62.1	10,374	53.5
$25,000 or more	10,866	27.5	2,309	11.9
Total	40,702	100.0	20,894	100.0
AGE				
Less than 35	14,588	35.8	9,095	43.5
35 and over	26,133	64.2	11,800	56.5
Total	40,702	100.0	20,894	100.0
HOURS				
Less than 2000	7,525	18.5	5,481	26.2
2000 and over	33,176	81.5	15,413	73.8
Total	40,702	100.0	20,894	100.0
SEX				
Women	16,335	40.1	9,932	47.5
Men	24,367	59.9	10,963	52.5
Total	40,702	100.0	20,894	100.0
TENURE[e]				
Less than 5 years	10,613	28.0	8,328	51.3
5 to 9 years	9,734	25.7	3,958	24.4
Ten years and over	17,518	46.3	3,830	23.6
Total	38,017	100.0	16,116	100.0

[a]Includes workers with no coverage, workers who do not know whether they have coverage and workers with no coverage information reported.

[b]Percentages exclude 12.7 percent of employees for whom firm size is not known.

[c]Includes workers who are not covered by a union contract, workers who do not know whether they are covered under a union contract, and workers with no reported information on unionization.

[d]Percentages exclude 4.4 percent of employees whose earnings are not reported.

[e]Total excludes 11.2 percent of employees who have worked at their current job for less than one year, doesn't include d/r.

SOURCE: Preliminary tabulations of EBRI/HHS May 1983 CPS pension supplement.

TABLE 4

The Use of Preretirement Lump-Sum Distributions
by Purpose and Amount
(as Reported May 1983)

	Total	less than $5,000	$5,000 - $9,999	$10,000 - $19,999	Over $20,000
TOTAL RECIPIENTS[a] (000's)	6,594	5,533	583	218	154
Percent Distribution[a]	100.0%	84.2%	8.9%	3.3%	2.3%
ALL USES[b]	100.0%	100.0%	100.0%	100.0%	100.0%
Total Saving	32.0%	26.0%	57.6%	78.9%	87.3%
Retirement Program	4.4	2.4	*	*	*
Insurance Annuity	*	*	*	*	*
Housing Purchase	10.1	9.3	12.5	*	*
Other Investment	16.8	14.0	29.9	45.9	*
Total Consumption	71.4%	76.6%	51.9%	42.6%	*
Car Purchase	4.8	4.8	*	*	*
Vacation	3.2	3.1	*	*	*
Other Use	63.4	68.7	40.9	*	*

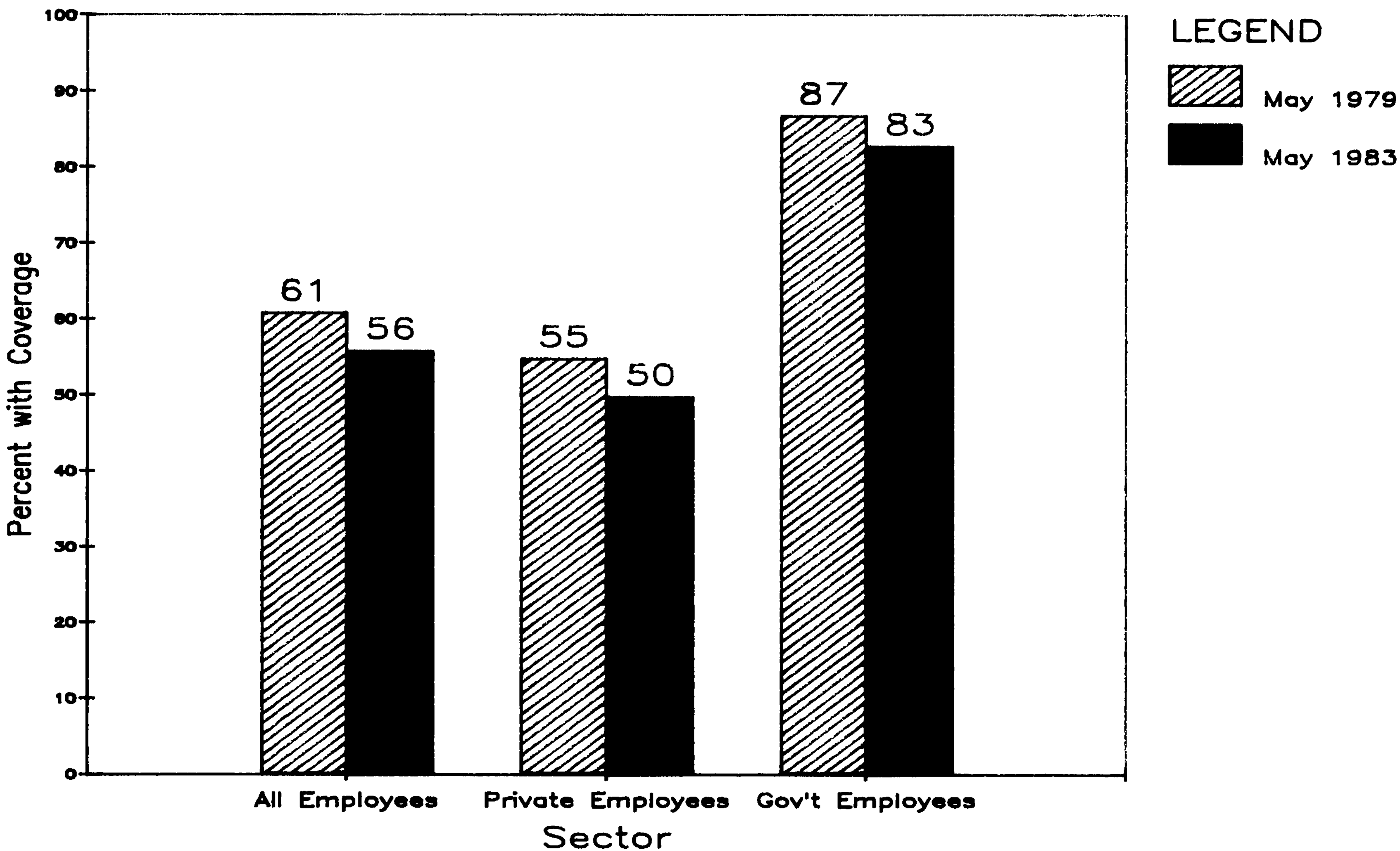
a Recipients by lump sum amount are less than total recipients and percentages are less than 100 percent because of the omission of "don't know" and "no response" to the survey question on the value of the lump-sum distribution.

b Percentages may add to over 100 percent because recipients may have used lump sum distribution in more than one way.

* Number of workers too small for rates to be calculated reliably.

Chart 1

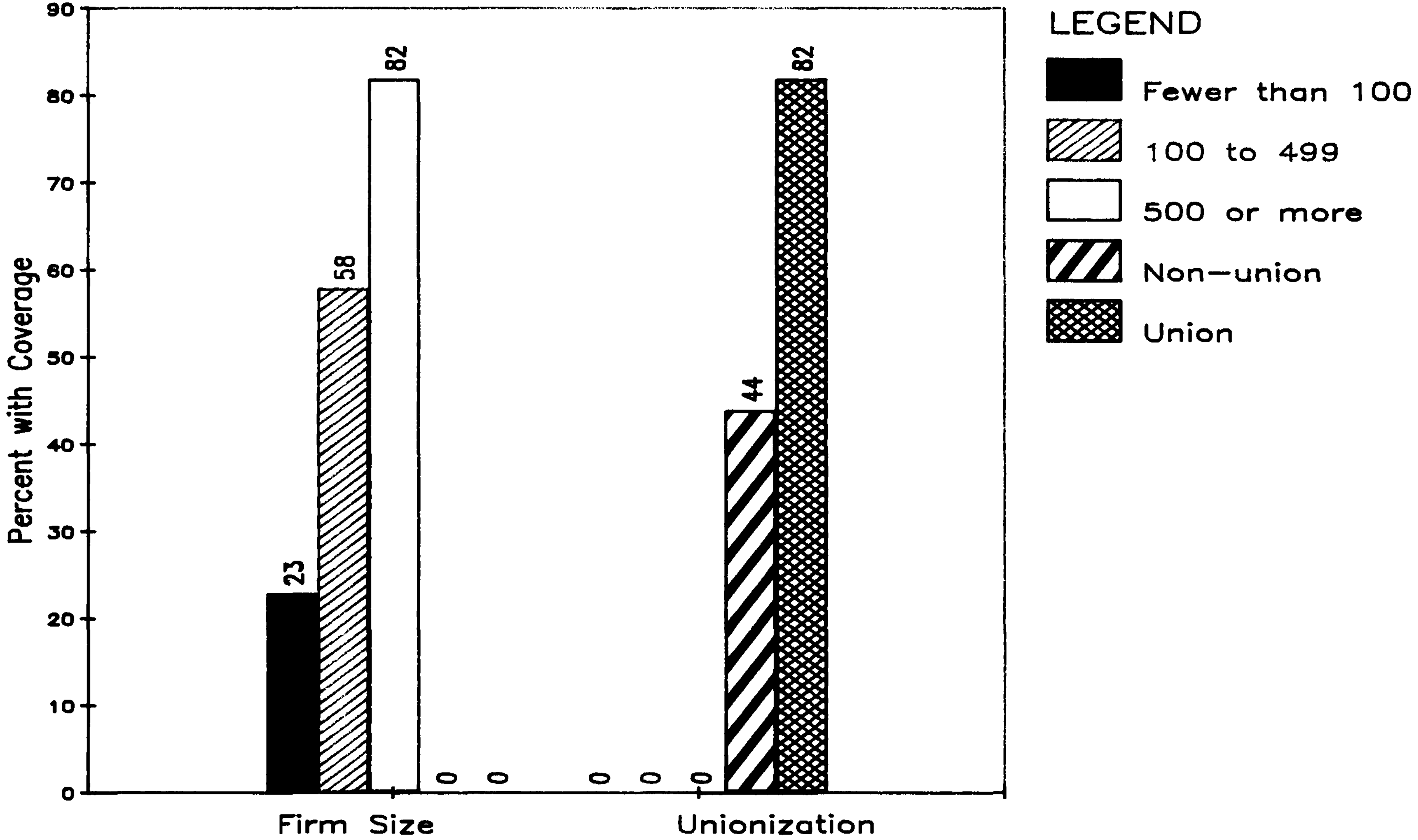
Percent of Non—Farm Workers with Pension Coverage, by Sector, May 1979 and May 1983



Source: Employee Benefit Research Institute

Chart 2

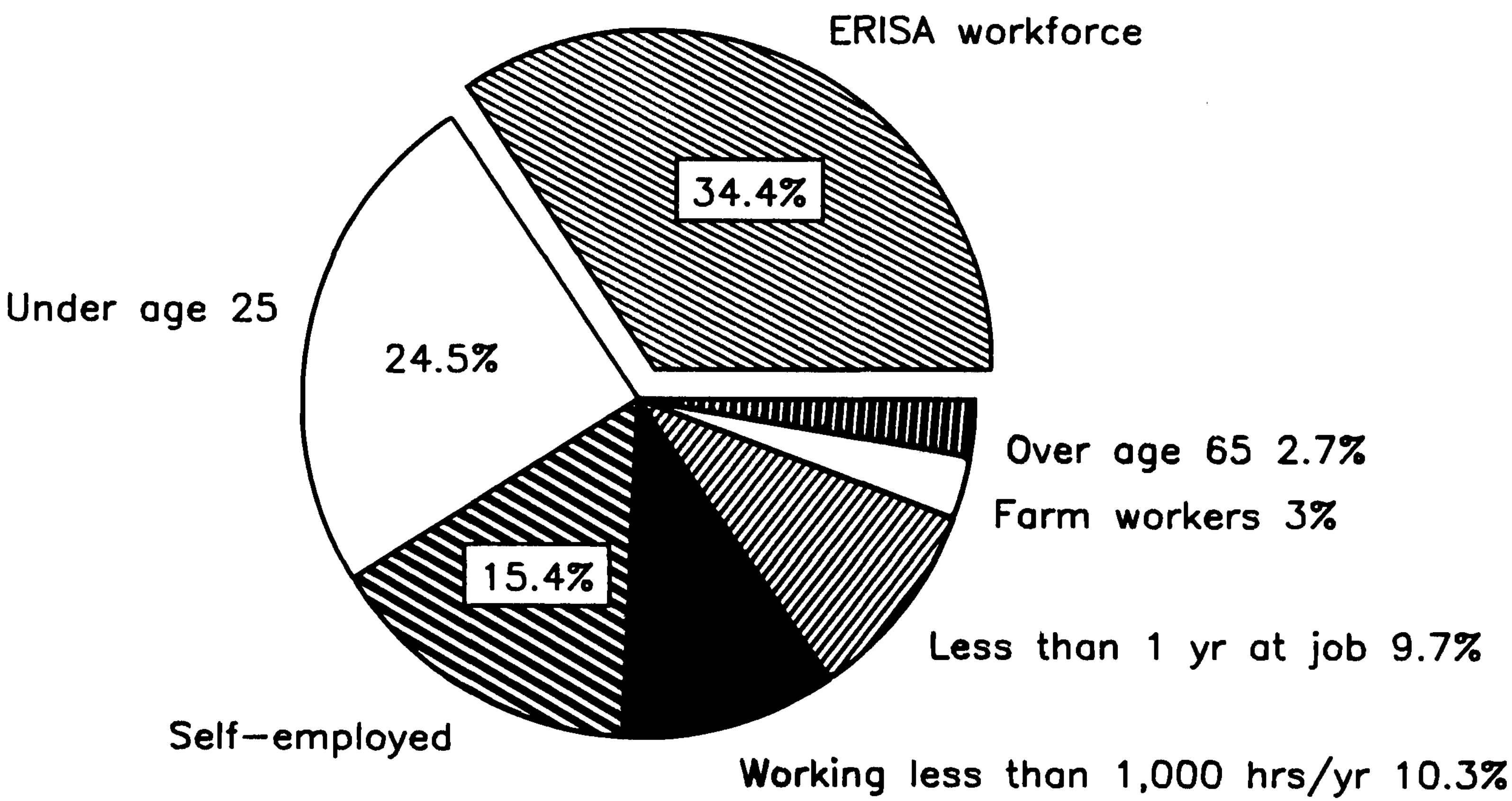
Percent of Non-Farm Private Employees with Pension Coverage, by Firm Size and Unionization, May 1983



Source: Employee Benefit Research Institute

Chart 3

Percent Distribution of Employees Lacking Pension Coverage Across Employment Categories, May 1983



Source: Employee Benefit Research Institute

Note: "ERISA workforce" consists of all employees not included in other categories (employees meeting ERISA participation standards).

TABLE 3

THE DISTRIBUTION OF COVERED AND NONCOVERED WORKERS
IN THE "NEAR-ERISA" WORKFORCE
AGES 25 THROUGH 64 WORKING 1000 HOURS OR MORE
BY SELECTED CHARACTERISTICS, MAY 1983

	Covered Workers (000's)	Distribution Across Groups	Workers Not Covered[a] (000's)	Distribution Across Groups
FIRM SIZE[b]				
Less than 100 employees	6,215	17.4%	12,352	68.1%
100 to 499 employees	5,545	15.6	2,465	13.6
500 or more employees	23,869	67.0	3,314	18.3
Total	40,702	100.0	20,894	100.0
UNION STATUS				
Union	15,223	38.2	2,163	10.6
Nonunion	24,627	61.8	18,155	89.4
Total	40,702	100.0	20,894	100.0
EARNINGS[d]				
Less than $10,000	4,107	10.4	6,711	34.6
$10,000 to $24,999	24,545	62.1	10,374	53.5
$25,000 or more	10,866	27.5	2,309	11.9
Total	40,702	100.0	20,894	100.0
AGE				
Less than 35	14,588	35.8	9,095	43.5
35 and over	26,133	64.2	11,800	56.5
Total	40,702	100.0	20,894	100.0
HOURS				
Less than 2000	7,525	18.5	5,481	26.2
2000 and over	33,176	81.5	15,413	73.8
Total	40,702	100.0	20,894	100.0
SEX				
Women	16,335	40.1	9,932	47.5
Men	24,367	59.9	10,963	52.5
Total	40,702	100.0	20,894	100.0
TENURE[e]				
Less than 5 years	10,613	28.0	8,328	51.3
5 to 9 years	9,734	25.7	3,958	24.4
Ten years and over	17,518	46.3	3,830	23.6
Total	38,017	100.0	16,116	100.0

[a]Includes workers with no coverage, workers who do not know whether they have coverage and workers with no coverage information reported.

[b]Percentages exclude 12.7 percent of employees for whom firm size is not known.

[c]Includes workers who are not covered by a union contract, workers who do not know whether they are covered under a union contract, and workers with no reported information on unionization.

[d]Percentages exclude 4.4 percent of employees whose earnings are not reported.

[e]Total excludes 11.2 percent of employees who have worked at their current job for less than one year, doesn't include d/r.

SOURCE: Preliminary tabulations of EBRI/HHS May 1983 CPS pension supplement.