FACTS from EBRI

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U.S. Retirement Income System

History

- The first public-sector retirement income plan was the New York City Teachers Retirement Plan, which was set up in 1869. The first private-sector retirement income plan was established by American Express Company in 1875. The federal government established the Civil Service Retirement System in 1920. A retirement income plan for military personnel was not funded until 1984.

Significant federal legislation affecting retirement income plans:

- 1921—The Revenue Act of 1921 exempted from current taxation interest income on trusts holding stock bonus or profit-sharing plans. Under this act, trust income was taxed as it was distributed to employees only to the extent that it exceeded employees' own contributions. The act did not authorize deductions for past service contributions.
- 1926—The Revenue Act of 1926 exempted income of pension trusts from current taxation.
- 1928—The Revenue Act of 1928 allowed employers to take tax deductions for reasonable amounts paid into a qualified trust in excess of the amount required to fund current liabilities. It changed the taxation of trust distributions that are attributable to employer contributions and earnings.
- 1935—The Social Security Act was signed into law.
- 1942—The Revenue Act of 1942 tightened standard qualifications for pension plans, limited allowable deductions, and allowed integration of plans with Social Security.
- 1948—The National Labor Relations Board ruled that Congress intended pensions to be part of wages and to fall under "conditions of employment" mentioned in the act, although the term was not specifically defined.
- 1974—The Employee Retirement Income Security Act of 1974 (ERISA) was passed. It was designed to secure the benefits of participants in private pension plans through participation, vesting, funding, reporting, and disclosure rules, and established the Pension Benefit Guaranty Corporation (PBGC). ERISA provided added pension incentives for the self-employed (through changes in Keoghs) and for persons not covered by pensions (through individual retirement accounts (IRAs)). It established the legal status of employee stock ownership plans (ESOPs) as an employee benefit, codified stock bonus plans under the Internal Revenue Code (IRC), and established requirements for plan implementation and operation.
- 1978—The Revenue Act of 1978 established qualified deferred compensation plans (sec. 401(k)) under which employees are not taxed on the portion of income they elect to receive as deferred compensation rather than direct cash payments. It created simplified employee pensions (SEPs) and changed IRA rules.
- 1996—The Small Business Job Protection Act of 1996 created the savings incentive match for employees (SIMPLE) for small establishments.
- 1997—The Taxpayer Relief Act of 1997 created a new, nondeductible IRA, the Roth IRA, which can be used to save for retirement, first-time home purchase, and college expenses. More individuals are eligible for a Roth IRA than for a deductible IRA.

For more details on the history of pension plans, see www.ebri.org/facts/0398afact.htm

Types of Retirement Income Plans

- Most retirement income plans are employment-based. There are two basic types of retirement income plans: defined benefit (DB) and defined contribution (DC).

- In a DB plan, benefits are calculated according to a formula or rule. Formulas are more common and are usually based either on years of service and a percentage of pay or on a negotiated flat-dollar amount. Benefit levels, as determined by the formula, are guaranteed as a stated retirement income commencing at a specified age. Although retirement benefits are usually expressed as a life annuity, lump-sum distributions are increasingly available.

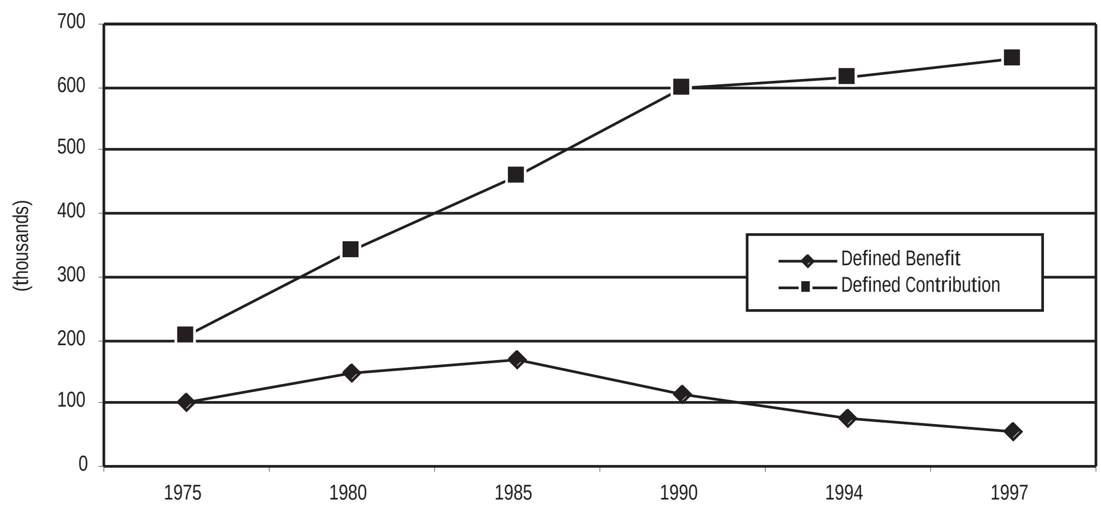
- In a DC plan, contributions are allocated to individual accounts according to a predetermined formula. Individual benefits are equal to account contributions (less any unpaid loans or withdrawals) and investment returns thereon, and are usually paid in the form of a lump-sum distribution. The benefit can also be paid as a life annuity at retirement if the employer offers this option.

- Another distinction among retirement income plans is whether the plan sponsor is a private-sector employer or a public-sector employer (federal, state, and local governments). The distinction between public and private sector is important because of the different environments in which they operate. Public-sector retirement income plans are products of a legislative process. Private-sector sponsors, while strongly affected by the legislative process, are relatively free to establish, maintain, and modify their plans. Because of the federal nature of the U.S. political system, federal regulation of state and local government plans has evolved over time. State and local government plans are heavily regulated through the IRC. State and local governments are exempt from ERISA's reporting, disclosure, and funding requirements (Title I) and termination insurance (Title IV).

Number of Plans

- One of the most discussed trends in retirement income plans is the declining number of DB plans and the increasing number of DC plans. Data on this trend exist only for the private sector. The reporting requirements of ERISA make it possible to obtain an accurate count of the number of private sector plans operating in a given year. In 1975, the number of DB plans was 103,346. This number increased to 170,172 by 1985. Since 1985, the number of DB plans has steadily declined. EBRI estimates that in 1997 there were 53,000 private-sector DB plans. Over the same time period, 1975–1997, the number of DC plans steadily increased from 207,748 to an estimated 647,000.

Number of Private-Sector Defined Benefit and Defined Contribution Plans, 1975-1997



Number of Retirement Plans 1950–1997

	1950	1960	1970	1975	1980	1985	1990	1994	1997
Private Industry	a	a	a	311,094	488,901	632,135	712,308	690,344	700,000
Defined benefit	a	a	a	103,346	148,096	170,172	113,062	74,422	53,000
Defined contribution	a	a	a	207,748	340,805	461,963	599,245	615,922	647,000
State and Local Governments[b]	a	2,346	2,304	3,075	3,075	2,589	2,387	a	a
Federal Government	2	2	2	2	2	2	4	4	4

[a]Data not available.
[b]Because of data availability, past years for state and local governments do not match with other categories. The data years for state and local governments apply to the years in the table headings: 1960 is represented with 1962 data, 1970 is represented with 1971–1972 data, and 1975 is represented with 1976–1977 data, 1980 is represented with 1981 data.

- The reasons for this trend are complex. One factor becomes apparent when the trend is viewed by plan size. The vast majority of plan terminations have occurred among the very small DB plans, those with two to nine active employees. Some suggest that the very small plans were top-heavy plans used by employers as tax shelters. The decline in the number of these DB plans is thought to be a result of federal legislation passed in the 1980s, most notably the Tax Equity and Fiscal Responsibility Act of 1982 and the Tax Reform Act of 1986.

- Studies have shown that the net increase in the number of DC plans is greater than the net decrease in the number of DB plans. This suggests that the growth in the number of DC plans is a result of something other than a shift from DB to DC plans.

- For more details on the trend in the number of DB and DC plan, see www.ebri.org/store/ebriib.htm or order the October 1997 *Issue Brief*.

Participation

- As the American work force has grown, so has the number of individual participants in employment-based retirement income plans. Total participation in private-sector retirement income plans increased from 44.5 million in 1975 to an estimated 86.0 million in 1997. In the following table, total participation includes employees currently participating in their employers' plans (also includes double-counting of individuals who are participating in more than one plan with their current employer if more than one plan is offered), employees who have left employment with an employer and have chosen to leave the assets in that employer's plan, and individuals who are currently retired and receiving benefits from a retirement income plan.

Total Retirement Plan Participants 1950–1997

	1950	1960	1970	1975	1980	1985	1990	1994	1997[a]
					(millions)				
Private Industry	b	b	b	44.5	57.9	74.7	76.9	85.1	86.0
Defined benefit	b	b	b	33.0	38.0	39.7	38.8	40.3	40.0
Defined contribution	b	b	b	11.5	19.9	35.0	38.1	44.8	46.0
State and Local Governments[c]	b	5.4	9.1	11.0	14.7	15.2	16.9	13.3	b
Federal Government	b	b	b	b	6.4[d]	8.6	10.7	10.8	b

[a]Estimates.
[b]Data not available.
[c]Because of data availability, past years for state and local governments do not match with other categories. The data years for state and local governments apply to the years in the table headings: 1960 is represented with 1962 data, 1970 is represented with 1971–1972 data, 1975 is represented with 1976–1977 data, and 1980 is represented with 1981 data.
[d]Data are for 1981.

- Active participants are those individuals who are participating in an employment-based retirement income plan that is sponsored by the employer they are presently working for.

- Active participation increased among private-sector employees at an average annual rate of 6.7 percent between 1950 and 1960. This rate of increase slowed over time. From 1960 to 1970, it was 3.5 percent; from 1970 to 1990, it was 3.2 percent; from 1980 to 1990, it was 1.6 percent; and from 1990 to 1997, it was 1.0 percent.

- By comparison, rates of increase among active participants in the Social Security program were lower than the participation rate among private-sector employees. From 1950 to 1960, the rate of increase of individuals covered by Social Security was 4.1 percent; from 1960 to 1970, it was 2.5 percent; from 1970 to 1980, it was 2.0 percent; and from 1980 to 1990, it was 1.7 percent.

- Among state and local government employees, the average annual rate of increase in active retirement income plan participation from 1960 to 1970 was 5.3 percent. This was higher than the participation rate among private-sector employees. The average annual rate of increase among state and local government employees slowed to 2.1 percent between 1970 and 1980. From 1980 to 1990, the rate of increase was 0.9 percent.

Active Retirement Plan Participants 1950–1997

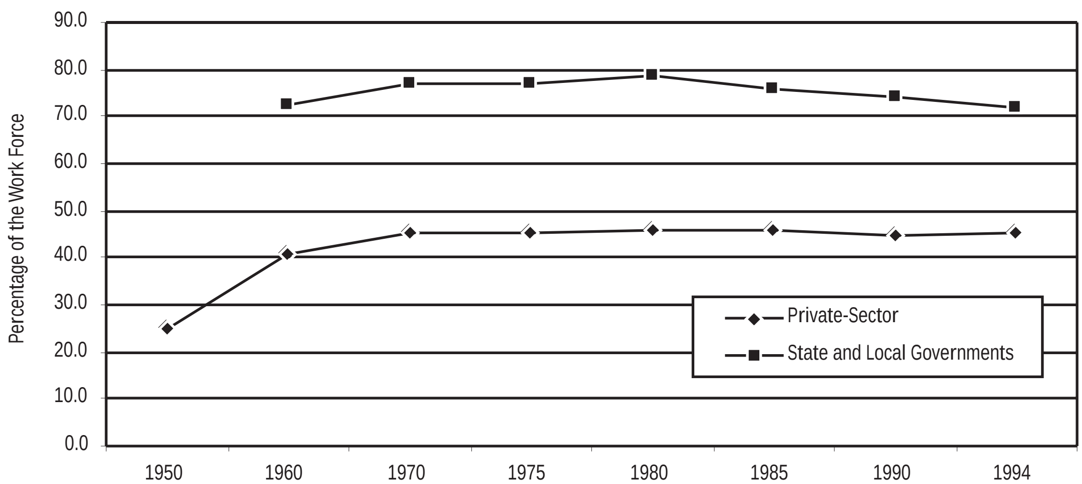
	1950	1960	1970	1975	1980	1985	1990	1994	1997[a]
					(millions)				
Private Industry	9.8	18.7	26.3	30.7	35.9	40.4	42.0	45.5	45.0
Defined benefit	b	b	b	26.8	29.7	28.9	26.3	24.6	25.0
Defined contribution	b	b	b	3.9	6.2	11.6	16.1	20.9	20.0
State and Local Governments[c]	b	5.0	8.4	9.7	10.3	10.4	11.3	11.8	b
Federal Government	b	b	2.7	2.7	3.0	5.0	6.0	6.4	b
Social Security	48.3	72.5	93.1	100.2	113.0	119.8	133.6	138.0[a]	b

[a]Estimates.
[b]Data not available.
[c]Because of data availability, past years for state and local governments do not match with other categories. The data years for state and local governments apply to the years in the table headings: 1960 is represented with 1962 data, 1970 is represented with 1971–1972 data, 1975 is represented with 1976–1977 data, and 1980 is represented with 1981 data.

- The percentage of all private-sector workers who participated in a retirement income plan remained fairly constant from 1970 to 1997, at around 45 percent.

- The percentage of all state and local government workers who participated in a retirement income plan remained fairly constant from 1960 to 1997, at around 75 percent. Among private-sector employees there was a sharp increase from 1950, when 25.0 percent of all private-sector workers participated in a retirement income plan, to 1960, when 40.8 percent participated in a retirement income plan. From 1960 to 1994, participation in a retirement income plan among all private-sector workers remained fairly steady, ranging from 40.8 percent to 45.1 percent.

Active Retirement Plan Participants as a Percentage of the Work Force, 1950 - 1994



Active Retirement Plan Participants as a Percentage of the Work Force 1950–1994

	1950	1960	1970	1975	1980	1985	1990	1994
Private Industry	25.0%	40.8%	45.1%	45.1%	45.9%	45.8%	44.8%	45.1%
Defined benefit	a	a	a	39.4	38.0	32.7	27.8	24.3
Defined contribution	a	a	a	5.8	7.9	13.1	17.0	20.7
State and Local Governments[b]	a	72.4	76.7	77.2	78.8	75.8	74.3	72.0

[a]Data not available.
[b]Because of data availability, past years for state and local governments do not match with other categories. The data years for state and local governments apply to the years in the table headings: 1960 is represented with 1962 data, 1970 is represented with 1971–1972 data, 1975 is represented with 1976–1977 data, and 1980 is represented with 1981 data.

Assets

- The total amount of assets held in various retirement plans has increased substantially over the years. In 1950, $21.6 billion was held in all retirement income plans. By 1995, this amount had increased to $6,845.4 billion. The following table also shows assets held in the Social Security Old Age and Survivors Insurance trust fund at the end of each year. These assets are not reflected in the “Total Assets” line because of the unique nature of the trust fund financing. Social Security assets are shown here for comparison purposes and for completeness because of the program’s central importance to so many Americans’ retirement income.

- Several factors account for the increase in retirement plan assets. The increase in the number of employees participating in a plan necessarily increases the amount of assets held by these plans. From 1950 to 1997, diversity in the types of retirement income plans increased, exemplified most notably by 401(k) plans, created in 1978, and IRAs, created in 1974 as part of ERISA.

Retirement Plan Assets 1950–1997

	1950	1960	1970	1975	1980	1985	1990	1995	1997
					($ in billions)				
Total Assets	$21.6	$86.7	$236.1	$473.3	$1,030.7	$2,341.2	$4,088.0	$6,845.4	a
Private trusteed	7.1	38.1	112.0	260.0	563.6	1,207.1	1,571.9	2,656.5	3,579.1
defined benefit	a	a	a	186.0	401.5	814.0	948.0	1,414.0	1,888.0
defined contribution	a	a	a	74.0	162.1	417.0	690.0	1,236.0	1,636.0
Private insured	5.6	18.9	40.8	70.1	158.2	346.7	636.1	782.1	889.5
State and local governments	4.9	19.7	60.3	104.8	196.6	398.7	920.0	1,517.8	2,049.1
Federal government[b]	4.0	10.0	23.0	38.4	73.7	154.0	326.0	537.0	a
IRA/Keogh plans	a	a	a	a	38.6[c]	234.7	634.0	1,352.0	1,948.0
Social Security	13.7	20.3	32.5	37.0	22.8	35.8	214.2	458.5	589.1

[a]Data not available.
[b]Data for the federal government's retirement plans are for civilian employees only until 1985. The Military Retirement System was unfunded until October 1, 1984.
[c] 1981 data.

For more information, contact Ken McDonnell, (202) 775-6342, or see EBRI's Web site at www.ebri.org.
Source: *EBRI Databook on Employee Benefits*, fourth edition, 1997, *Fundamentals of Employee Benefit Programs*, fifth edition, 1997, and Kelly Olsen and Jack VanDerhei, "Defined Contribution Plan Dominance Grows Across Sectors and Employer Sizes, While Mega Defined Benefit Plans Remain Strong: Where We Are and Where We Are Going." *EBRI Issue Brief* No. 190/*Special Report SR-33* (October 1997).

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