Fundamentals of Private Pensions

by

DAN M. McGILL, Ph.D.

Associate Professor of Insurance and
Research Director, Pension Research Council
Wharton School of Finance and Commerce

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To
Elaine Kem McGill
Pension Research Council

C. A. Kulp, Chairman, Insurance Department
Wharton School of Finance and Commerce

Harry Becker, Professor of Hospital Economics, Northwestern University, Chicago
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S. S. Huebner, Emeritus Professor of Insurance and Commerce,
Wharton School of Finance and Commerce
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M. A. Linton, Chairman of the Board, Provident Mutual Life Insurance Company, Philadelphia
Ben S. McGiveran, Seefurth and McGiveran, Pension Underwriters, Chicago and Milwaukee
Fred P. McKenzie, Vice-President, The Hanover Bank, New York City
J. W. Myers, Manager, Insurance and Social Security Department,
Standard Oil Company of New Jersey, New York City
Ray M. Peterson, Vice-President and Associate Actuary, Equitable Life Assurance Society of the United States, New York City
Otto Pollak, Associate Professor of Sociology, Wharton School of Finance and Commerce
George F. Sisler, Vice-President, First National Bank, Chicago
D. N. Warters, Executive Vice-President, Bankers Life Company, Des Moines

Dan M. McGill, Research Director
Associate Professor of Insurance
Wharton School of Finance and Commerce
Purpose of the Council

The Pension Research Council of the Wharton School was created in 1952 for the purpose of sponsoring nonpartisan research in the area of private pensions. It was formed in response to the urgent need for a better understanding of the private pension movement. Private pensions have experienced a phenomenal growth during the last two decades, but their economic, political, and social implications are yet to be explored. They seem destined to play a major role in the quest for old-age economic security, but the nature of that role can be ascertained only on the basis of a more enlightened evaluation of the capabilities and limitations of the private pension mechanism. It was to conduct an impartial study into the facts and basic issues surrounding private pensions, under the auspices of an academic and professional group representing leadership in every phase of the field, that the Council was organized.

Projects undertaken by the Council will be broad in scope and predominantly interpretive rather than technical in nature. In general, attention will be concentrated on areas which are not the object of special investigation by other research groups. Its research studies will be conducted by mature scholars drawn from both the academic and business spheres. Research results will be published from time to time in a series of books and monographs.
Preface

This volume is the initial publication of the Pension Research Council of the Wharton School of Finance and Commerce. It has a twofold purpose: (1) to provide a broad background for the more specialized studies to follow and (2) to serve as a basic text for those persons aspiring to a fuller understanding of the private pension mechanism. It is especially designed to meet the needs of college or university students and trainees in insurance companies, trust companies, and pension consulting firms. It should also prove useful to management personnel, labor union representatives, and others interested in the administration of private pensions.

In keeping with the fundamental objectives of the book, an effort has been made to strike a proper balance between principles and practices. It is in no sense a manual for the pension technician. The emphasis is on why rather than how. Naturally, a great deal of attention has been devoted to how pension plans operate, but the general approach of the book is to analyze—plan provisions, funding media, and funding methods—not to advocate. This is true of even the last chapter which presents a critique of the principal funding media. Attention is focused on the factors which should be considered, not on absolute or final answers.

No consideration has been given to profit-sharing plans and other forms of deferred compensation. While such plans are widely used to provide retirement benefits either alone or in conjunction with a conventional pension plan, their characteristics are so distinctly different from those of pension plans as to warrant their exclusion from this treatise.

As is true of any undertaking of this scope, the author is indebted to many persons and organizations for counsel and assistance. The magnitude of his debt is evidenced by the fact that a minimum of thirty pension specialists, half of them actuaries, read all or a portion of the manuscript before it went to the printer and offered many valuable criticisms and suggestions. The manuscript was reviewed in its entirety by most of the members of the Council and, in many
Preface

instances, by their pension associates. The author hereby acknowledges his indebtedness to all persons who reviewed the manuscript and expresses his deepest gratitude for their cooperation and his sincerest regrets that space considerations make it impracticable to mention all by name.

Some rendered such valuable assistance that they deserve especial recognition. Mr. John K. Dyer, Jr., Vice-President and Actuary of Towers, Perrin, Forster, and Crosby, Inc., gave generously of his time and counsel and was particularly helpful in connection with actuarial matters. Mr. Preston C. Bassett, Associate Actuary with the same organization, performed extensive actuarial calculations for the author and reviewed large sections of the manuscript. Mr. Ray M. Peterson, Vice-President and Associate Actuary of the Equitable Life Assurance Society of the United States, read the entire manuscript and acted as adviser on group annuity practices. Messrs. Dennis N. Warters, William M. Rae, and Charles L. Trowbridge, Executive Vice-President, Group Secretary, and Associate Group Actuary, respectively, of the Bankers Life Company of Iowa, offered many perceptive criticisms and were especially helpful in the area of group permanent insurance practices. Mr. Laflin C. Jones, C.L.U., Director of Insurance Services and Planning, and his associates at the Northwestern Mutual Life Insurance Company, provided constructive criticism on all phases of the manuscript, with particular emphasis on pension trust or individual contract matters.

Dr. Roger F. Murray, Vice-President of Bankers Trust Company, read the original draft of the manuscript and made numerous suggestions, with special attention to trust company investment operations. Mr. J. W. Myers, Manager, Insurance and Social Security Department, Standard Oil Company of New Jersey, read the entire manuscript and drew upon his rich experience in pension administration to suggest many worthwhile changes. Mr. Robert J. Myers, Chief Actuary of the Social Security Administration, Federal Security Agency, reviewed for factual accuracy the material in Chapter I relating to the economic basis of the old-age problem and governmental pension plans.

The weightiest acknowledgment of all should go to Mr. Ben S. McGiveran, C.L.U., of Seefurth and McGiveran, who not only has contributed generously from his vast storehouse of pension knowledge but was the person who conceived the idea of what is now the
Pension Research Council and assumed primary responsibility for securing the necessary financial support. Special thanks should also go to those individuals and organizations, too numerous to mention, who have participated in a financial way and without whose public-spirited support the project could not have been undertaken.

The private pension field is highly competitive and strong differences of opinion exist with respect to certain practices in the field and particularly with regard to the relative merits of the various funding media. These differences of opinion are reflected within the membership of the Council. It is emphasized, therefore, that the views expressed in this volume are those of the author and are not to be imputed to any other member of the Council or to any other person whose assistance is cited in this preface. Likewise, any factual errors that may still be found in the book are the sole responsibility of the author.

March, 1955
Philadelphia, Pennsylvania

D. M. M.
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The private pension movement is rooted in one of the most significant economic, social, and political developments of the twentieth century—the progressive aging of the population. This development has given rise to a multitude of problems, the most pressing of which, unquestionably, is that of providing a measure of economic security to the aged. Some conception of the magnitude of the problem can be grasped from the following brief account of the gerontological and economic influences at work.

ECONOMIC BASIS OF THE OLD-AGE PROBLEM

POPULATION TRENDS

During the last half-century, the growth in the number and proportion of the aged population has been phenomenal. During that period the general population of the United States has doubled, while the number of persons age 65 and over has quadrupled. In 1900, there were roughly three million persons age 65 and over, whereas fifty years later the number had grown to 12½ million. The aged population is increasing at the rate of 340,000 per year, which means that at the end of 1954, there were approximately 13.9 million aged persons in the population. It is estimated that by the year 2000, aged persons will number 26 to 28 million. In relative terms, only 4 per cent of the population in 1900 was 65 and over, whereas at the end of 1954, 8.5 per cent of the population fell in that category. Moreover, if present trends continue, from 11 to 13 per cent of the population will be 65 and above by the year 2000.

2 Underlying Forces

This spectacular increase in the absolute and relative number of old persons in the United States reflects the combined influence of a decline in the birth rate, an increase in life expectancy, and the curtailment of immigration. The long-run decrease in the birth rate was reversed during World War II and has remained at a relatively high level since that time, but population experts are reluctant to predict the future course of fertility. The tremendous extension in life expectancy recorded during the last fifty years as a result of advances in medical science, particularly in the control of infectious diseases and the reduction of infant mortality, improvements in public health services, and a rise in general living standards, will certainly not be duplicated during the next half-century, but as medical science devotes more and more study to the diseases of old age, further gains in life expectancy can be anticipated. Immigration, which once contributed large numbers of young people to the United States population, has been a negligible factor for the past twenty-five years and is not expected to assume a more important role in the future.

Employment Opportunities for the Aged

The increase in the proportion of old people has been accompanied by a decline in the employment opportunities of the aged. In 1890, the aged constituted 3.9 per cent of the total population and 4.3 per cent of the total labor force. By 1952, the percentage of the population age 65 and over had more than doubled, but the percentage of the total labor force age 65 and over had barely increased. In 1890, 39.9 per cent of all persons age 65 and over were in the labor force, while in 1952 only 23.4 per cent were in that category. This decline has taken place chiefly among aged males. In 1890, 70 per cent of such males were in the labor force, but by 1952 the percentage had shrunk to 40.9 per cent. The rate of female participation in the labor force declined only slightly during that period, from 8.5 per cent to 8.0 per cent.

Many factors have contributed to the decline in labor force participation by the aged, but one of the most significant, without question, has been the transition from an agrarian and essentially

rural economy to an industrial and predominantly urbanized economy. Whereas persons in agricultural employment can continue working, at least on a part-time basis, to advanced ages, industrial employees, because of the physical demands of their jobs or employer personnel policy, must retire at a relatively early age. Other factors which have influenced the trend include the improvement in longevity, extension of social insurance and pension programs, and the institutionalization of age 65 as the normal retirement age.

Capacity to Save for Old Age

The implications of the foregoing are broadened by the lessened capacity of individuals to save for their own old-age maintenance. Several developments within the last quarter-century have magnified the difficulties of accumulating an old-age estate. Frequently overlooked in this connection are the technological changes that have taken place during such period. A greatly improved and expanded industrial plant is pouring forth a vastly increasing quantity of consumer goods, of infinite variety, exerting relentless pressure on all classes of individuals to spend all or the greater portion of their income. High-pressure advertising and liberal extension of installment credit have conspired to tie up the worker's income even before it is earned. As a result, systematic provision for old age has become a secondary consideration in the budget calculations of the majority of families.³

A second factor that has complicated the accumulation of an estate is the inexorable rise in personal and corporate income taxes. The stupendous fiscal needs of the Federal government, traceable to war and the threat of war, have led to the imposition of personal tax rates which at the upper income levels approach the point of confiscation and render it difficult for even those persons in the higher income brackets to make adequate provision for their old-age needs. High corporate tax rates have added to the problem.

A third factor has been the corrosive influence of price inflation. This phenomenon requires no documentation but does inspire the comment that inflation impairs the ability of fixed-income persons to save a portion of their income and undermines the purchasing

³. It may be argued that this development reflects a weakened propensity to save for old age rather than a lessened capacity.
power of funds which have already been accumulated by any group of income recipients.

Finally, the economic dependency of many persons now in the aged category was precipitated by the depression of the 1930's which swept away their savings and shrunk their opportunities for economic rehabilitation.

The composite effect of such developments is unmistakably apparent in recent surveys of the personal financial resources of the aged. Information on the net worth of all age groups in the population is made available through the periodic Surveys of Consumer Finances conducted by the Board of Governors of the Federal Reserve System in cooperation with the Survey Research Center of the University of Michigan. The 1953 survey revealed that the median net worth of spending units headed by persons aged 65 and over was $8,400.4 Inasmuch as 69 per cent of the units headed by persons age 65 and over owned their homes, however, it may be presumed that a substantial portion of the median net worth is represented by the value of the home. Nevertheless, home ownership is not to be discounted, since it reduces the cash needs of aged persons and may produce some income. Retired persons, as contrasted with those age 65 and over, had a median net worth of only $6,000. While these statistics indicate that elderly people as a group are far from destitute—a picture of their economic circumstances painted in some quarters—it is obvious that the resources of the great majority of elderly persons are not adequate to provide even a subsistence income for life.

Surveys by the Social Security Administration of the income, assets, and living arrangements of the beneficiaries of the Old-Age and Survivors Insurance program tend to confirm the findings of the Board of Governors. A survey of such beneficiaries at the end of 1951 disclosed that about two-thirds of the married men owned their homes, 80 per cent of them free from mortgage.5 About 60 per cent of the beneficiaries had some savings in addition to their home. Only 13 per cent, however, had as much as $5,000 in savings, apart

4. Federal Reserve Bulletin, September, 1953, p. 942. A spending unit is defined as all persons living in the same dwelling and belonging to the same family who pool their incomes to meet their major expenses.
from their homes. Approximately 25 per cent of the beneficiaries had no assets whatsoever.

CHANGED CONCEPT OF FILIAL RESPONSIBILITY

In earlier days it was not a matter of particular concern if persons reached old age without adequate means of support. Elderly members of a family resided with and were supported by younger members of the family. In many cases, the elderly persons were able to perform some tasks around the household, or farm, thus lightening the burden on the younger people. With increasing urbanization of society, changes in housing conditions, and many other economic and social developments, the traditional approach to old-age care and support has become outmoded. As a result society is looking increasingly to Government and employers for old-age support.

PUBLIC PENSION PROGRAMS

The limitations of the individual approach to old-age financial security have led to the establishment of various governmental programs of old-age income maintenance. The most comprehensive and significant undertaking of this sort is the Federal Old-Age and Survivors Insurance system. This program has such a profound impact on private pension plans that careful consideration should be given to its structure and underlying philosophy.

FEDERAL OLD-AGE AND SURVIVORS INSURANCE

Coverage.—Federal Old-Age and Survivors Insurance is the national program of old-age insurance created by the Social Security Act of 1935 and, as such, is the foundation of all other programs of old-age income maintenance. Unlike many national programs of old-age insurance, including those of Canada and Great Britain, OASI is not based on the principle of universal coverage. Rather, coverage is conditioned on attachment to the labor market. The broad objective of the program is to cover all gainfully employed persons, including the self-employed. With minor exceptions, coverage for all eligible persons is compulsory and immediate. In other words, OASI is a device by which gainfully employed persons are
6 Underlying Forces

forced by statute to assume some responsibility for their own old-age maintenance.

As to the technique of coverage, the plan covers by exclusion rather than by inclusion. That is, all gainfully employed persons are covered except those specifically excluded. The original legislation, however, excluded some important groups, the most significant being self-employed persons, domestic servants, agricultural workers, casuals, railroad workers, governmental employees, and employees of educational, religious, and charitable organizations. Based on administrative and constitutional considerations, these exclusions withheld coverage from four out of every ten gainfully employed persons.

The exclusion of such a formidable proportion of employed persons introduced serious inequities into the program and what was even more important tended to frustrate the basic objective of the program. Therefore, in 1950 the coverage was extended to many of the previously excluded groups, bringing an additional ten million persons under the system. At the same time, the concepts of optional coverage (for employees of state and local governments and non-profit organizations) and qualifying conditions as to regularity of employment (for domestics, farm laborers, and casuals) were introduced. The scope of the program was further broadened in 1954 through compulsory coverage of all self-employed persons who had not been brought under coverage by the 1950 Act, except members of the legal and medical professions, extension of optional coverage to additional groups, and the liberalization of qualification requirements for domestic and farm labor. Today nine out of every ten gainfully employed persons are covered under the system.

Benefits.—

a. Eligibility for Benefits.—The benefits payable under the OASI program are paid as a matter of statutory entitlement and are not conditioned on a showing of need. The quasi-contractual nature of the program not only avoids the administrative complications of a needs test but protects the privacy of the individual and preserves his self-respect. Equally important, it encourages the individual to accumulate savings to supplement the benefits of the OASI program and any other retirement plan of which he might be a member. Retirement benefits are payable upon actual retirement at or after
age 65 and the satisfaction of a service requirement. An individual is entitled to retirement benefits only if he has been credited with forty quarters of coverage or, alternatively, coverage equal to half of the calendar quarters that have elapsed since December 31, 1950 (or age 21, if later) up to age 65, subject to a minimum of six quarters. An individual who has met such service requirements is said to be "fully insured." If he has achieved that status through forty quarters of coverage, he is permanently as well as fully insured and will retain that status even though he may spend no further time in covered employment. It might be said that the benefits vest after ten years of service (a shorter period for those over age 45 on January 1, 1951), subject to diminution through periods of non-coverage or lower earnings.

Prior to the 1950 amendments to the Social Security Act, a person's insured status was determined by the period since January 1, 1937. The extension of coverage produced by that legislation was accompanied, in the interest of equity, by a "new start" arrangement under which any person, including those previously covered, could become fully insured with six quarters of coverage. This enabled those persons who were within a few years of retirement to qualify for benefits on the basis of service and earnings since 1950. The extension in 1954 was not accompanied by another "new start," since only four years had elapsed since the previous one and, moreover, a new "drop out" provision (explained below) accomplishes roughly the same objective.

As stated above, benefits are conditioned on actual retirement, the test of which has been withdrawal from covered employment. Under the 1939 Act an otherwise eligible claimant was disqualified for benefits for any month in which he earned wages in covered employment of $15 or more. In 1950, the earnings limit was eliminated for persons age 75 and over and raised to $50 for all other persons. In 1952, the limit was increased to $75. Finally, in 1954,

6. A quarter of coverage is any calendar quarter in which an employed person earns at least $50 in covered employment or any quarter in a calendar year in which he earns $4200 in covered employment. A self-employed person is credited with four quarters of coverage in any year in which he earns at least $400.

7. Any individual who reaches age 65 in a fully insured status, or achieves such status subsequently, is also permanently insured, even though he may not have acquired forty quarters of coverage.
an annual limitation of $1200 was substituted for the $75 monthly limitation, and the age below which the limitation is applicable was lowered to 72. The law now provides for suspension of one monthly benefit for each $80, or fraction thereof, of annual earnings in excess of $1200. In no case, however, are benefits withheld for any month in which the beneficiary’s remuneration as an employee was $80 or less, and in which he rendered no substantial services in self-employment. On the other hand, all earnings, not just covered earnings, are now taken into account.

Incorporated in the law in the first instance as a device for forcing older workers out of a depressed labor market, the earnings limitation has been retained primarily to hold down the cost of the OASI program. It was estimated prior to the 1954 amendments that the payment of benefits to all fully insured persons at age 65 would increase the cost of the program by 13 per cent. Complete elimination of the earnings limitation today would increase current outlays under the program by $1 billion per year. It is difficult to justify expenditures of such magnitude to persons who have not actually retired, particularly in view of the burdensome level which the cost of the program will eventually reach.

b. Nature of Benefits.—The OASI program provides both retirement and survivorship benefits, all of which are based on the insured’s “primary insurance amount,” whose derivation is described below. The insured’s retirement benefit, a life income, is designated the “old age insurance benefit” and is identical with the primary insurance amount. The wife of a retired worker is entitled to a benefit equal to 50 per cent of the primary insurance amount if she is 65 or over, or, irrespective of her age, if she has under her care a dependent and unmarried child of the insured under age 18. Furthermore, each dependent and unmarried child under 18 is entitled to a benefit equal to one-half of the primary insurance amount. The combined family benefits, however, may not exceed $200 per month, or 80 per cent of the insured’s average monthly wage (see below), whichever is smaller.

Prior to the 1939 amendments to the Social Security Act, no survivorship benefits, other than a lump-sum payment, were avail-

able under the OASI program. That legislation not only authorized survivorship benefits but created a special category of insured persons to facilitate the payment of such benefits. Survivorship benefits are now available if the deceased were "currently insured," a status which can be attained with six quarters of coverage, all of which, however, must have been earned within the thirteen quarters preceding the date of death, including the quarter in which death occurs. The same benefits are available if the deceased were "fully insured," a matter of some importance since a person may be "fully insured" without being "currently insured." In addition to a lump-sum benefit equal to three times the primary insurance amount, or $255, whichever is smaller, income benefits are payable to widows age 65 and over, mothers of any age who have dependent children of the deceased under their care, dependent children under 18 and, if there are no other eligible income beneficiaries, dependent parents 65 and over. Dependent widowers age 65 and over are also entitled to benefits if the deceased were both "currently" and "fully insured."

c. Level of Benefits.—All benefits payable under the OASI program are based on the insured's covered earnings, specifically, on his average monthly wage. The average monthly wage is a technical concept and with some administrative refinements, is obtained by dividing the insured's total covered wages, which since 1954 include all wages in covered employment up to a maximum of $4,200 per year, by the number of months that have elapsed since January 1, 1951, or the day preceding the year in which the insured reached age 22, whichever is later. Prior to 1954 all months after the stipulated date were included in the divisor, whether or not the individual had covered earnings in those months. The 1954 amendments, however, provide that up to five years of lowest or no earnings may be dropped out in the calculation of the average monthly wage. In addition, those quarters during which an insured individual is unable to earn income because of a condition of total disability are to be omitted from the denominator in the calculation of the average monthly wage.

The benefit formula is heavily weighted in favor of the lower-income worker. Under the original average wage formula, the

9. The law provides a four-year "drop out" for those insured persons with less than twenty quarters of coverage and a five-year "drop out" for those with twenty or more quarters of coverage.
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primary benefit was equal to 40 per cent of the first $50 of average monthly wage plus 10 per cent of the excess, up to a maximum monthly wage of $250, multiplied by 1 per cent for each calendar year in which the insured earned at least $200 in covered employment. Successive revisions of the formula have increased the proportion of the average monthly wage reflected in the primary insurance amount until at present the benefit is equal to 55 per cent of the first $110 of average monthly wage and 20 per cent of the excess up to $350 of average monthly wage. The application of this formula produces a maximum primary insurance amount of $108.50, and the law prescribes a minimum of $30. The 1 per cent increment, designed to recognize length of service, was eliminated in 1950 on the theory that the method of calculating the average monthly wage gives adequate recognition to length of service.

Financing.—To the present, the cost of the OASI program, including both benefit and administrative expenditures, has been borne by the covered employees and their employers. The funds have been derived from a payroll tax levied in equal proportions on employers and employees. The original Act was based on the theory that the program should be self-supporting, and a schedule of contributions designed to accomplish that objective was set forth in the Act. The schedule, which called for an initial contribution rate of 1 per cent of covered wages on the part of both the employer and employee, presumed the accumulation of a large reserve, somewhat comparable to the funding of private pension plans. The advisability—and feasibility—of a large reserve was subsequently questioned and, pending a determination of the issue, Congress postponed year after year the scheduled increases in the contribution rate. Finally, in 1950, the rate was permitted to go to 1½ per cent each, or 3 per cent combined, and a new rate schedule was projected, calling for an ultimate combined rate of 6½ per cent of covered earnings by 1970. With the liberalization of the benefit formula in 1954, the contribution schedule was again revised upward, with the rate scheduled to go to 4 per cent each in 1975. The present rate of contribution is 2 per cent each for wage earners and their employers, and 3 per cent for self-employed persons.

The present system of financing is neither a pay-as-you-go nor full-reserve plan. Contributions have been more than adequate to
meet benefit and administrative expenditures but less than adequate to accumulate a full reserve. The expenditures of the program in 1954, its eighteenth year of operations, amounted to less than 3 per cent of covered payroll, while in the same year contributions equaled 4 per cent of payroll. The excess contributions have led to the accumulation of a trust fund, or reserve, of more than $20.5 billion. Yet it has been estimated that this fund would not be capable of meeting the obligations of the program to those persons who have already begun to draw old-age benefits, not to mention the accrued liabilities for those persons who are still working. Indeed, official estimates as of the end of 1953, based on the provisions then in effect, placed the present value of the benefits to be paid to those persons already on the OASI benefit rolls at $23 billion and the total accrued liability of the system, including that for all persons who have contributed to the program, at $200 billion. The accrued liability is substantially higher today in view of the liberalization of benefits in the 1954 amendments.

**Federal Staff Retirement Plans**

Entirely distinct from the national old-age insurance program, several staff retirement plans have been established under the aegis of the Federal Government. Designed, with one notable exception, to provide old-age benefits to various categories of Federal employees, these plans bear a close resemblance to private pension plans. Employees enrolled under these plans are not concurrently covered under OASI, although partial integration with OASI has been achieved with respect to the Railroad Retirement System.

Largest of the Federal plans and, in fact, the largest single employer pension plan in existence, is the Civil Service Retirement System, which provides retirement and survivorship benefits to career employees of the Federal Government. Established in 1920, the plan now covers about 1.5 million employees. Participation is compulsory for all eligible employees. During the calendar year 1953, 190,600 persons, on the average, were drawing retirement benefits from the system and another 50,400 were receiving survivorship benefits. Approximately one million Federal employees

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without permanent civil service status are included in the OASI program.

In addition to the Civil Service Retirement System, there are nine other retirement plans covering Federal civilian employees. Some of the more important plans cover members of the foreign service, employees of the Federal Reserve Banks, employees of the Tennessee Valley Authority, and members of the Federal judiciary. Most of these plans provide more liberal benefits than those of the Civil Service Retirement System.

On the periphery of Federal staff plans is the Railroad Retirement System. This program is unique in the American pension field in that it is operated for a group of private employees but is underwritten by the Federal Government. It was established by the Railroad Retirement Act of 1937 in an attempt to restore financial stability to the various individual railroad plans which were threatened with insolvency after years of difficulties. Protection is provided against the five major hazards to economic security—old age, disability, death, unemployment, and sickness—and the benefits are guaranteed by the Federal Government.¹²

STATE AND LOCAL RETIREMENT SYSTEMS

A heterogeneous assortment of public pension plans has been established at the state and local level. These plans differ widely in their details, but in most jurisdictions separate plans exist for policemen, firemen, and teachers, all other employees, if covered at all, being lumped together into a general retirement system. Because of the hazardous nature of their work, policemen and firemen were the earliest groups of public employees to obtain retirement benefits, and up to the present, plans for such employees have contained more liberal provisions than those for other public employees. As a rule, police and firemen plans provide for low employee contributions, retirement at an early age after relatively brief service (typically twenty years), liberal survivors' benefits, disability benefits, and retirement benefits based on compensation for the highest grade held. Teacher

retirement systems are less liberal than the policemen and firemen funds, but even so they usually accord more generous treatment than the plans maintained for rank-and-file employees.

Approximately 1700 in number, state and local plans are characterized by low benefits, long service requirements, nontransferability of credits, and inadequate financing.

NONCONTRIBUTORY PENSION PROGRAMS

Noncontributory pension programs represent another broad source of old-age benefits and deserve brief mention. The best known of these programs is Old Age Assistance, which came into existence with the enactment of the Social Security Act and was broadly designed to complement the old-age insurance scheme which is now termed OASI. It was intended that Old Age Assistance should provide benefits to those indigent old persons who could not qualify for insurance benefits, or who could qualify but for one reason or another would not receive adequate benefits. This objective was to be accomplished through a system of Federal grants-in-aid to states which already had or would establish old-age assistance programs which could meet certain standards prescribed in the law. Conceived as a transitional device, the program has shown no tendency to diminish in importance and continues to rival OASI in number of beneficiaries and dollar value of benefit expenditures. The Federal Government is currently bearing about 53 per cent of benefit expenditures and one-half of the costs of administration.

Other noncontributory pension benefits are provided by the Veterans Administration and the regular military establishments.

THE PRIVATE PENSION MOVEMENT

RATIONALE

Industrial pensions appeared on the American scene during the last quarter of the nineteenth century, but only within the last two decades have they assumed any significance in the old-age financial picture. In the beginning, private pension benefits were universally regarded as gratuities from a grateful employer in recognition of long and faithful service. The payments were usually discretionary,
the employer assuming no legal obligation to provide benefits. In fact, most plans stated in specific terms that no employee rights were being created thereunder and reserved to the employer the right to deny benefits to any employee and to reduce or terminate benefits which had already commenced. A few plans promised to continue benefit payments to retired employees but made no commitment to active employees.

As the years went by, certain groups, anxious to encourage and strengthen the pension movement, sought to place on the employer a moral obligation to provide pensions to superannuated employees. As early as 1912, one student of the old-age problem wrote: “From the standpoint of the whole system of social economy, no employer has a right to engage men in any occupation that exhausts the individual’s industrial life in ten, twenty, or forty years; and then leave the remnant floating on society at large as a derelict at sea.” This point of view was frequently expressed during the next few decades, being the subject of widespread debate in the early 1920’s. It was adopted by the United Mine Workers and used by that organization in its 1946 campaign to establish a welfare fund. The union’s position has been expressed by its President as follows:

The United Mine Workers of America has assumed the position over the years that the cost of caring for the human equity in the coal industry is inherently as valid as the cost of the replacement of mining machinery, or the cost of paying taxes, or the cost of paying interest indebtedness, or any other factor incident to the production of a ton of coal for consumers’ bins . . . [The agreement establishing the Welfare Fund] recognized in principle the fact that the industry owed an obligation to those employees, and the coal miners could no longer be used up, crippled beyond repair and turned out to live or die subject to the charity of the community or the minimum contributions of the state. The concept received its most influential endorsement in the report of the fact-finding board in the 1949 steel industry labor dispute. The board wrote, in part, as follows:

As hereinafter amplified, we think that all industry, in the absence of adequate Government programs, owes an obligation to workers to provide for maintenance of the human body in the form of medical and similar

benefits and full depreciation in the form of old-age retirement—in the same way as it does now for plant and machinery.\textsuperscript{15}

And again:

... the steel companies have, with some exceptions, overlooked the fact that the machines and plant on which the industry has prospered, and on which it must depend in the future, are not all made of metal or brick and mortar. They are also made of flesh and blood. And the human machines, like the inanimate machines, have a definite rate of depreciation.\textsuperscript{16}

Despite its respectable following, this concept, now known as the Human Depreciation Concept, clearly rests on some logical imperfections. In the first place, aging is not a result of employment but of physiological processes. Even if it could be established that certain occupations tend to accelerate the aging process, the employer logically should be responsible for only the increase in the rate of aging. Secondly, the responsibility for providing retirement benefits is placed entirely on the last employer. Only the terminal employer is accused of casting away the worn out human machine, leaving it “floating on society at large as a derelict at sea.” The same disapprobation does not attach to an employer who discharges an employee in his middle years without providing paid-up pension benefits. Finally, and this is the crux of the matter, the cost of replacing a human machine is not comparable to that of replacing a physical machine. A human machine can be replaced with only the cost of training a replacement, whereas the purchase price of a new unit must be accumulated to replace a worn out physical machine.\textsuperscript{17}

The Human Depreciation Concept has been supplanted—or supplemented—in some quarters, by the theory that pensions are nothing more than deferred wages. The latter concept holds that an employee group has the prerogative of choosing between an immediate wage increase and a pension plan, and, having chosen the latter, is entitled to regard the benefits as deferred wages. Like the

\textsuperscript{15} Steel Industry Board, \textit{Report to the President of the United States on the Labor Dispute in the Basic Steel Industry}, September 10, 1949, p. 55.

\textsuperscript{16} Ibid., p. 64.

\textsuperscript{17} Of course, if social pressure forces an employer to provide old-age support for his employees, he will have to accumulate a capital sum for each employee or provide for such maintenance out of current earnings. In such event, the replacement of a superannuated employee would be comparable to the replacement of a worn out machine.
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Human Depreciation Concept, this point of view found early expression:

Theoretically, the simplest way of dealing with labor would be the payment of a money wage, requiring the employee to provide for the hazards of employment and his old age. While here and there an employee does this, by and large the mass of employees do not.

In order to get a full understanding of old-age and service pensions, they should be considered as a part of the real wages of a workman. There is a tendency to speak of these pensions as being paid by the company, or, in cases where the employee contributes a portion, as being paid partly by the employer and partly by the employee. In a certain sense, of course, this may be correct, but it leads to confusion. A pension system considered as part of the real wages of an employee is really paid by the employee, not perhaps in money, but in the foregoing of an increase in wages which he might obtain except for the establishment of a pension system.\(^{18}\)

Pursued to its logical conclusion, this concept has some far-reaching implications. Certainly it would call for full, immediate vesting of all benefits in the employees. It would also require that the minimum employer contribution to the plan be equal to the proposed wage increase. (As a matter of fact, the concept usually carries the implication that the employer should assume the full cost of the plan.) Finally, it might be argued, as Dearing does,\(^{19}\) that all contributions should be paid into an irrevocable trust fund administered by the employees, entirely free of either employer or union control.

The unions which quite naturally are the most articulate advocates of this concept have not insisted on its rigorous application to specific bargaining situations. In fact, many inconsistencies are found between theory and practice. Perhaps the most basic inconsistency is the almost universal absence of any vesting provisions in negotiated pension plans. Furthermore, there is rather general insistence on union participation in the administration of the plan, jointly with the employer, as opposed to unfettered administration by the employee group. Nevertheless, the concept assumes a certain realism when the cost of the pension plan is translated into cents per hour


and the employer averts a wage increase by agreeing to a pension plan.

It is doubtful that the private pension movement can be explained in terms of any one social or economic philosophy. Its rationale lies in broad and conflicting forces that do not lend themselves to definitive characterization. One might conclude that the only tenable explanation of the development is business expediency. Yet this expression is so pervasive that it furnishes only the vaguest of clues as to the specific forces that motivate employers to adopt pension plans. It might be helpful, therefore, to examine some of the significant factors and developments that have made it seem expedient to an employer to establish a pension plan.

Forces Influencing the Growth of Private Pension Plans

Productivity of the Employee Group.—Unquestionably, one of the most compelling employer motives in adopting a pension plan is the desire to increase the productivity of his employees. This motive is usually mixed with others, including a sincere desire to provide financial security to retired or superannuated employees. Nevertheless, unless the employer believes that the cost of the pension plan can be substantially offset by savings in other phases of company operations, including production costs, he may not be overly receptive to the idea of pensions.

On balance there is little doubt that the efficiency of the labor force is enhanced through the establishment of a pension plan. American industrial development has reached the stage where most concerns of any size now face or will soon face the problem of dealing with large numbers of employees near or beyond normal retirement age. This problem may be handled in one of three ways. The first possible approach is for the employer to discharge his employees without retirement benefits as they become superannuated. With Federal OASI benefits available in increasingly generous proportions, such action would not be as callous as it might otherwise be. Nevertheless, in the present state of social consciousness, most employers shun such an approach, not only for humanitarian reasons but because of the risk of public censure. A second possibility is for the employer to retain his superannuated employees on the payroll at full or reduced pay but in a capacity commensurate
with their diminished ability and vitality. This policy is usually disruptive of employee morale and may prove to be uneconomical in other respects. The third approach, and in the great majority of cases the only one offering a satisfactory solution, is for the employer to establish a formal pension plan. This permits the employer to remove over-age employees from the payroll in an orderly fashion, without fear of adverse employee and public reaction, and to replace them with younger, presumably more efficient, workers. The inevitable result is a more productive work force.

The installation of a pension plan is thought to boost production in other ways. It is argued, for example, that the morale of the employee group will be elevated through the elimination of the workers' anxiety over their old-age security, not to mention the favorable attitude engendered by such tangible evidence of the employer's concern for the welfare of his employees. While a pension plan is definitely a positive morale factor, one may wonder whether its influence among the rank and file employees, particularly those distant from retirement, is not overshadowed by more immediate considerations, such as wages, hospitalization benefits, and working conditions.

It is also argued that the establishment of a pension plan will reduce turnover and hence the cost of training replacements. This argument is difficult to evaluate, since it is impossible to isolate the influence of a pension plan from the other factors that have a bearing on turnover. It is of some pertinency to point out that the highest rate of turnover occurs among employees who because of their youth or short service may not be eligible for membership in the plan, or even if active participants, may be only slightly influenced in their choice of employment by the promise of a retirement benefit many years in the future. Moreover, it should be remembered that any reductions in turnover will be reflected in higher pension costs, since a higher percentage of employees will qualify for severance or retirement benefits.

A pension plan is a particularly effective instrument of personnel policy with respect to supervisory employees. Supervisory personnel represent a more stable and permanent group of employees, to whom the promise of a pension appears less illusory than to the hourly workers. They tend, therefore, to be more responsive to the stimulus
of a pension plan and to carry out their responsibilities more effectively. Furthermore, since the responsibilities of the supervisory personnel are, by definition, on a higher level than those of the ordinary employee, it is especially important that a means exist whereby the executives and other supervisors can be readily retired when they have passed the peak of effectiveness. Related to this is the importance of keeping open the channels of promotion. In a large organization, one retirement can precipitate a chain of promotions—all to the betterment of employee morale and efficiency. Finally, a pension plan unquestionably enables an employer to attract and hold better qualified executives than would otherwise be possible. This is particularly true of those firms which normally draw their executives from external rather than internal sources.

_Tax Inducements._—Related to the foregoing in the sense that both are cost-reducing factors are the tax inducements offered by the Federal Government. The Revenue Act of 1942 is frequently—and erroneously—cited as the genesis of the favorable tax treatment of private pension plans, but the real beginning of such policy is found in much earlier legislation. As a matter of fact, before the enactment of any legislation directed specifically at private pensions, reasonable payments made by an employer, as pensions to retired employees or as contributions to a trust to fund current pension credits, were deductible from the employer’s gross income for tax purposes. Such payments were deductible only as an ordinary and necessary business expense and then only if, together with other payments, they represented reasonable compensation. However, payments to a trust to fund liabilities for past service credits or to place the trust on a sound financial basis were not deductible. Moreover, the income of the trust was currently taxable to the employer, employees, or the trust, depending on the provisions of the trust instrument.

The latter condition was removed by the Revenue Act of 1921, which exempted from current taxation the income of a trust created by an employer as part of a stock bonus or profit-sharing plan for the exclusive benefit of some or all of his employees. The income of pension trusts was not exempted by statute from current taxation until the enactment of the Revenue Act of 1926, but by administrative ruling pension trusts were accorded the same status as stock
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bonus and profit-sharing trusts after 1921. In all cases, the income was to be taxable to the employees when actually distributed or made available.

Inasmuch as the Revenue Act of 1921 did not authorize deductions for past service contributions or contributions to establish the financial soundness of a plan, many employers adopted the practice of carrying balance sheet reserves against their pension obligations. Credits to these reserves were not deductible in arriving at net taxable income. The increase in the number and size of such reserves led to the enactment of a provision in the Revenue Act of 1928 which permitted an employer to take deductions for reasonable amounts paid in to a qualified trust in excess of the amounts required to fund current liabilities. In effect, this meant that an employer could transfer his balance sheet reserve to a trust or make other payments to a trust for the purpose of funding past service liabilities. However, deductions for any contributions in excess of the amount required to fund current service credits had to be apportioned in equal parts over a period of ten years. While this was a reasonable requirement when the past service liability was liquidated in one year, it was burdensome and unduly complicated when only a portion of the past service liability was funded each year, with each portion having to be spread over a ten-year period. It is interesting to note that this limitation on past service contributions did not apply to plans funded through group annuities, such discrimination existing until 1942 when all plans were made subject to the limitations of Section 23(p) of the Revenue Act of that year.

Unfortunately, as the law stood after 1928, pension plans lent themselves to tax-avoidance schemes. This was made possible through two broad loopholes in the law. In the first place, a pension trust could qualify for favorable tax treatment if it were created for the exclusive benefit of "some or all of the employees." Thus, the owners and officers of close corporations could establish a plan for the benefit of themselves and perhaps a few key employees, gaining an immediate tax deduction for the corporation without an immediate tax to themselves as participants. In the second place, the law did not require that the trust be irrevocable. An employer could make substantial contributions to a trust during years of high earnings, taking deductions against his income tax, and then recapture the earnings in poor years by revoking the trust. This practice not
only deprived the Government of tax revenue but perhaps more important was detrimental to the interests of the participating employees.

Abuses under the law led to the inclusion of the so-called Non-Diversion Rule in the Revenue Act of 1938. This rule stated that it must be impossible at any time prior to the satisfaction of all liabilities under the trust for any part of the trust funds to be diverted to purposes other than the exclusive benefit of the employees. In brief, the trust had to be irrevocable. No attempt was made in that legislation, however, to broaden the participation in qualified plans, so that it remained possible to establish qualified plans for a few favored employees.

The impetus given to the adoption of pension plans by the sharp increase in corporate income taxes in 1940, and other influences, forced the Congress to tighten up the requirements for qualification. This was accomplished in the Revenue Act of 1942. The provisions of this Act, as subsequently amended, were re-enacted in the Internal Revenue Code of 1954 and, along with implementing regulations, constitute the law under which pension plans operate today.

At the present time, in order for an employer to deduct his contributions to a pension plan, whether for current or past service, the plan must meet the general requirements of Section 401(a) of the Internal Revenue Code of 1954 [Section 165(a) of the 1942 Code]. As implemented by Sec. 29.165 of Regulations 111, these requirements are:

(a) There must be a trust, contract, or other legally binding arrangement. The plan must be in writing and must be communicated to the employees. Furthermore, it must be a permanent and continuing program.

(b) The plan must be for the exclusive benefit of the employees or their beneficiaries, and it must be impossible prior to the satisfaction of all liabilities under the plan for any part of the corpus or income to be diverted to any other use. In fact, the trust agreement or other applicable document must contain a specific statement to the effect that no funds can be diverted.

(c) The plan must benefit employees in general and not just a limited number of favored employees. To meet this requirement
the plan must cover either a prescribed percentage of employees or a classification of employees found by the Commissioner of Internal Revenue not to be discriminatory in favor of officers, shareholders, supervisors, or highly compensated employees.\textsuperscript{20}

(d) The plan must not discriminate in favor of officers, shareholders, or highly compensated employees with respect to contributions or benefits. Variations in contributions or benefits are permissible so long as the plan in its over-all operations does not discriminate in favor of that class of employees with respect to which discrimination is prohibited. It is of special significance that contributions or benefits based on remuneration excluded from the OASI wage base may differ from contributions or benefits within such base so long as the resulting differences in benefits are approximately offset percentage-wise by the benefits available under the Federal OASI program. If such an equivalence obtains, the plan is said to be integrated with OASI.\textsuperscript{21}

(e) The plan must provide definitely determinable benefits. This requirement is designed to distinguish a pension plan from a profit-sharing plan. A plan to provide retirement benefits to employees or their beneficiaries will be deemed a pension plan if either the benefits payable to the employee or the contributions required of the employer can be determined actuarially. Benefits are not definitely determinable if funds arising from forfeitures on termination of service, or for other reasons, may be used to provide increased benefits for the remaining participants rather than being used to reduce employer contributions. There is an implication that the plan should be actuarially sound but as will be apparent from later discussions Treasury approval of a plan carries with it no certification that contributions under the plan will be adequate to provide the accrued benefits.

Contributions to a plan which qualifies under Section 401(a) are deductible under Section 404 of the Code [Formerly Section 23(p)]. In order to be deductible under Section 404, however, the contributions must fall within a class of expense deductible under Section 162 (relating to trade or business expenses) or Section 212 (relating to

\textsuperscript{20} See pp. 31-34 for a fuller explanation of the coverage requirement.

\textsuperscript{21} See pp. 42-48 for a more detailed explanation of the integration requirement.
expenses for the production of income). That is to say, contributions may be deducted under Section 404 only to the extent that they are ordinary and necessary expenses incurred in carrying on a trade or business or in the production of income and are in the nature of compensation for personal services actually rendered. In no case is a deduction allowable for a contribution on behalf of an employee in excess of an amount which, together with other deductions allowed as compensation for such employee's services, constitutes a reasonable allowance for compensation.

After employer contributions have qualified as ordinary and necessary expenses, they must conform to the detailed limitations contained in Section 404(1)(A) through (D). These limitations are dealt with at length at a later point and will not be discussed here.

In addition to the encouragement offered private pension plans through deductibility of employer contributions, the income of a qualified trust is exempted from Federal income taxation until disbursed in the form of benefits. Furthermore, employer contributions to a qualified plan are not taxable to the participating employees until actually received.

The deductibility of employer contributions has given rise to a general impression that the Government bears a share of the burden of providing pension benefits, a factor which has acted as a strong stimulus to the establishment of pension plans. This view was particularly prevalent during World War II when an excess profits tax was being levied in addition to the normal corporate income tax, the combined levy being 85.5 per cent at the top income bracket. The thesis that a corporation subject to the maximum levy could finance a plan with fifteen-cent dollars was universally accepted. As recently as 1953, before the postwar excess profits tax expired, many companies could logically conclude that their pension plan was costing them only eighteen cents per dollar of outlay.

This conclusion is based on the assumption that employer contributions come out of the top bracket of income and in the absence of a pension plan would go to the Government in the form of tax pay-

22. See pp. 133-36.

23. The taxability of employee benefits is a separate and involved subject which because of space limitations cannot be discussed here. It is not particularly relevant to the subject of employer motivation, except with respect to plans for management employees, where the primary incentive may be the deferred taxation of employer contributions.
ments. Such an assumption is undoubtedly valid in the short run, particularly during a period when prices and wage rates are virtually frozen, as they were during World War II. Other things being equal, any type of expenditure not incurred in earlier years or one that is increased over former years, reduces the net taxable income of the taxpayer by the amount of the expenditure and, in effect, is passed on to the Government in the proportion that the tax reduction bears to the increase in expenditures.

Other things do not remain equal indefinitely, however, and an expenditure that was marginal in one period may have become a permanent feature of the cost structure in the next period. In the long run, pension outlays may lose their marginal status and come to be regarded as a normal cost of labor, similar to wages and other benefits that go to employees. In such event an attempt will almost certainly be made to pass such costs on to consumers in the form of higher prices. Whether this can be done will depend on a number of variables, including the elasticity of demand for the company’s product, competition from other firms, and the nature of the industry.

To a considerable degree, the question of whether the pension contributions of a particular employer will be treated as a special outlay to be charged against profits or as an element of ordinary labor cost to be passed on to consumers will be determined by the extent to which pension plans are adopted and pension outlays are incurred by other firms in the industry or competing industries. So long as pension plans are established by only those firms with a better-than-average earnings record, employer contributions will undoubtedly have the effect of reducing profits and, hence, the tax liability of the firms. If, however, virtually all firms in an industry, including the marginal firms, should adopt plans, a situation might be created in which all employers could shift their pension costs to consumers.

Pressure From Organized Labor.—A third broad factor influencing the adoption of pension plans has been the attitude of organized labor. Until recently, organized labor was, in the main, either indifferent to the pension movement or openly antagonistic to it. Many of the older and well-established craft unions viewed
employer-sponsored pensions as a paternalistic device to wean the allegiance of the workers away from the unions to the employer. They also harbored a fear that pensions would be used to hold down wages. Over the years, however, these attitudes have changed to such an extent that in 1949, when another round of wage increases seemed difficult to justify, a large segment of organized labor demanded pensions in lieu of wages. The way was paved for such a switch when a Federal Court ruled that pensions are a bargainable issue.

This case arose out of a union grievance filed with the National Labor Relations Board in 1946, alleging that the unilateral action of the Inland Steel Company in enforcing a policy of compulsory retirement at age 65 constituted a breach of the provision of the general labor contract relating to separation from service. The grievance stemmed from the refusal of the company to negotiate the matter with the union on the grounds that compulsory retirement was an essential part of the company's pension plan and that pension plans did not fall within the scope of collective bargaining. The union did not contend that the provisions of a pension plan were of themselves subject to collective bargaining, but argued that the company could not take unilateral action with respect to any provision of a pension agreement that was also a part of the general labor contract and hence conceded to be within the scope of mandatory collective bargaining.

In 1948 the National Labor Relations Board ruled in effect that the Labor Management Relations Act of 1947 imposes a duty on employers to bargain with representatives of their employees on the subject of pensions. This decision was based on the dual premise that the term "wages" as defined in the statute includes any emolument of value such as pension or insurance benefits and that the detailed provisions of pension plans come within the purview of "conditions of employment" and therefore constitute an appropriate subject for collective bargaining.24

Upon appeal by the Company, the Seventh Circuit Court of Appeals approved the view of the National Labor Relations Board that the terms of a pension plan are subject to mandatory collective bargaining.

bargaining on the ground that they constitute "conditions of employment" but expressed some reservation with respect to the wage analogy:

We are convinced that the language employed by Congress, considered in connection with the purpose of the Act, so clearly includes a retirement and pension plan as to leave little, if any, reason for construction. While, as the Company has demonstrated, a reasonable argument can be made that the benefits flowing from such a plan are not "wages," we think the better and more logical argument is on the other side, and certainly there is, in our opinion, no sound basis for an argument that such a plan is not clearly included in the phrase, "other conditions of employment." 25

The Inland Steel Decision established a legal framework within which no employer can install, alter, or terminate a pension plan for organized workers without the assent of the labor bargaining unit. This obligation rests on the employer whether or not the plan was installed prior to certification of the bargaining unit and whether or not the plan be compulsory or voluntary, contributory or noncontributory.

The CIO took advantage of the new legal status of pensions to launch a concerted drive for pensions and other welfare benefits. The purpose of the drive was twofold: (1) to secure pension benefits directly from employers, and (2) to induce employers to join labor in seeking liberalization of the Federal OASI program. The CIO argued that the Federal program did not provide adequate benefits, a condition which they ascribed to the organized opposition of employers and insurance companies. By pressing for pension benefits to be financed entirely by management, union leaders felt that employers would be more receptive to proposals for liberalization of the Federal program which is jointly financed by management and labor. In line with this policy, the CIO agreed to deduction of OASI benefits from the benefits to be provided by the employer pension plan. The strategy was carried out through a unified collective bargaining program, the local unions being required to observe the standards prescribed by the governing bodies.

The CIO program does not reflect the views of all segments of organized labor. The AFoFL, for example, has urged more reliance on the Federal program, advocating employer plans for only those

workers whose wages provide a margin above the current necessities of life. It cautions against an ill-considered or poorly-designed plan, pointing out that "such a plan may impair other vital trade union aims and functions, while offering relatively little in return." Furthermore, the AFofL has made no attempt to impose a patterned pension program on its local unions. The locals have been given full discretion as to whether or not they will bargain with employers for pension coverage and, if so, as to what type of plan to seek. As a result, wide differences are found among the unions affiliated with the AFofL as to pension philosophy and practice.

Social Pressure.—A final factor that has encouraged the spread of pension plans is the social and political atmosphere that has prevailed during the last quarter-century. During that period the American people have become security-conscious. The economic upheaval of the early 1930's swept away the life savings of millions and engendered a feeling of insecurity that shook the very foundations of the country. Prominent among the proposals for economic reform were those that envisioned social action in the area of old-age income maintenance. The Federal OASI program was the outgrowth of these proposals.

Since the Federal program was deliberately designed to provide only a "floor of protection," the way was left clear for supplemental benefits to be provided through private measures. In view of the general inability—or unwillingness, as some would have it—of the individual to accumulate through his own efforts the additional resources required, society has come to expect the employer to bear a share of the burden. The employer may successfully shift his share of the costs to the consumer, but a great deal of social pressure is exerted on the employer to provide the mechanism through which additional funds can be accumulated. If the employer chooses not to install a formal pension plan, he may find that social pressure forces him to take care of his superannuated employees in some other manner. In anticipation of such a development, employers are turning in increasing numbers to formal pension programs as the most economical and satisfactory method of meeting the problem.

**PRESENT SCOPE**

Complete and up-to-date information on the number and coverage of private pension plans is not available. As of the end of 1953, there were 15,730 plans underwritten by life insurance companies, covering 3,940,000 employees. Individual contract pension trusts accounted for 10,470, or approximately two-thirds, of the plans but only 610,000, or about 15 per cent, of the persons covered. Group annuity contracts, comprising only one-fourth of the plans, accounted for more than 75 per cent of the coverage.

The number of self-administered trustee plans is not known. Estimates run as high as 5,000 plans. These plans cover an estimated 8,000,000 employees. This would mean that insured and self-administered plans combined cover 12,000,000 persons, or about 20 per cent of the current working population.

The following chapter indicates the range of provisions that may be found in these plans. Later chapters describe the legal arrangements, called funding media, under which the benefits of the plans may be provided; the actuarial techniques, called funding methods, that govern the rate at which the necessary funds are accumulated; and, finally, the factors which should be considered by the employer in selecting a funding medium.