The original documents are located in Box D34, folder "American Insurance Management Institute Regional Seminar, Columbus, OH, October 27, 1972" of the Ford Congressional Papers: Press Secretary and Speech File at the Gerald R. Ford Presidential Library.

M Office Copy

REMARKS BY REP. GERALD R. FORD, R-MICH.
REPUBLICAN LEADER, U. S. HOUSE OF REPRESENTATIVES

BEFORE THE AMERICAN INSURANCE MANAGEMENT INSTITUTE
REGIONAL SEMINAR

COLUMBUS, OHIO
FRIDAY MORNING, OCTOBER 27, 1972

It is indeed a pleasure to speak here today. Insurance is a fascinating field and also a very technical one. It's something every layman like myself needs to have some knowledge of, and yet it's difficult for me to get among pro's on the subject without fearing that I will be talked into buying something. Well, I don't have to worry about that today. All of us here are on the consumer side of the insurance business--only I'm sure you are much sharper at it than I am. Indeed, your organization must be one of the oldest consumer interest groups in the country.

I want to be careful that I don't lead you astray on what I came here to speak about. I didn't come here to speak about insurance--as you deal with it in your work--or to speak about consumerism--as we hear so much about it in the avant garde movement of today. I'm here to talk about private employee pension benefit plans. The debate on pension plans involves some ideas akin to insurance, some akin to consumerism, and some which emanate from the interests and prerogatives of management. So I wouldn't be surprised if many of you are already familiar with the pension issues. But let me add a few more ideas that are involved in the pension controversy. They include equity in the workplace, income adequacy of older Americans, Federal income tax, capital formation and concentration, and, as with many important domestic issues of today, the proper role of government regulation vis-a-vis the private decision-making process. In fact, there is hardly a domestic economic issue today which cannot be related in some way to our private pension system.

There are so many facets of the pension controversy and the pension plans themselves are so various and technically complicated that one could go on for hours simply describing the context of the issues. But I won't do that here because I think you already must have a good general knowledge of the subject. In the last year or so there have been many magazine and newspaper articles and at least two television "specials" devoted to the problems of the private pension system. What I would like to do in the brief time available here is to describe the President's program on pensions and the features of the two Administration

(more)

bills--one of which I introduced in the House of Representatives during the 92nd Congress.

Last December 8, President Nixon outlined his pension program in a message he sent to Congress. It is a five-point program which includes three new legislative proposals, a renewed endorsement of an earlier proposal, and a major study project which will provide the data needed to determine whether additional legislation should be recommended. Here are the essentials of the five points:

1. Employees who wish to save independently for their retirement or to supplement employer-financed pensions should be allowed to deduct on their income tax returns amounts set aside for these purposes.

Today only 30 million employes are covered by private retirement plans. Now I consider this fact--that about half of the private workforce has such coverage--to be a significant achievement and not at all a shortcoming. Nevertheless, the non-covered and independently covered workers should be encouraged to build up greater savings for retirement.

Under present law, both the contributions which an employer makes to a qualified private retirement plan on behalf of his employees and the investment earnings on those contributions are generally not subject to taxes until they are paid to the employee or to his beneficiaries. The tax liability on investment earnings is also deferred when an employee contributes to a group plan, though in this case the contribution itself is taxable. But when an employee saves independently for his own retirement, both his contribution and the investment earnings on such savings are currently subject to taxes.

This inequity discourages individual self-reliance and slows the growth of private retirement savings. It places an unfair burden on those employees (especially older workers) who want to establish a pension plan or augment an employer-financed plan. To provide such persons with the same opportunities now available to others, the Administration bill would make contributions to retirement savings programs by individuals deductible up to the level of $1500 per year or 20 per cent of income, whichever is less. Individuals would retain the power to control the investment of these funds, channeling them into bank accounts, mutual funds, annuity or insurance programs, government bonds, or into other investments as they desire. Taxes would also be deferred on the earnings from these investments.

This provision would be especially helpful to older workers who are most interested in retirement. The limitation on deductions would direct benefits primarily to employees with low

(more)

and moderate incomes, while preserving an incentive to establish employer-financed plans. The limit is nevertheless sufficiently high to permit older employees to finance a substantial retirement income. For example, a person whose plan begins at age 40, with contributions of $1500 a year, could still retire at age 65 with an annual pension of $7500, in addition to social security benefits.

This proposed deduction would be available to those already covered by employer-financed plans, but in this case the upper limit of $1500 would be reduced to reflect pension plan contributions made by the employer. An appropriate adjustment would also be made in the case of individuals who do not contribute to the Social Security system or the Railroad Retirement System.

2. Self-employed persons who invest in pension plans for themselves and their employees should be given a more generous tax deduction than they now receive.

Under present law, self-employed persons may establish pension plans covering themselves and their employees. However, deductible contributions are limited annually to $2500 or 10 per cent of earned income, whichever is less. There are no such limits to contributions made by corporations on behalf of their employees.

This distinction in treatment is not based on any difference in reality, since self-employed persons and corporate employees often engage in substantially the same economic activities. One result of this distinction has been to create an artificial incentive for the self-employed to incorporate; another result has been to deny benefits to the employees of those self-employed persons who do not wish to incorporate which are comparable to those of corporate employees.

To achieve greater equity, the Administration bill would raise the annual limit for deductible contributions by the self-employed to $7500 or 15 per cent of income, whichever is less. This provision would encourage and enable the self-employed to provide more adequate benefits for themselves and for their workers.

3. A minimum standard should be established for the vesting of pensions.

Inadequate vesting in pension plans is perhaps the most serious problem in our private pension system. Conceptually, vesting means that the benefit rights accrued by a plan participant will not be forfeited, even if he changes jobs or stops working before normal retirement age. When 10, 15, or 20 years of accrued pension credits suddenly go down the drain because of a layoff, illness, or opportunity for a better job, it is no consolation to be told that you have lost nothing because you never gained a legal right to a pension. The plain fact today is that, for the vast majority of plan participants, pension expectations are built up by going to work day in and day out, and not by hiring a lawyer and maybe also an actuary

(more)

to advise you from time to time about your status under the plan's provisions.

More than two-thirds of all private pension plan participants are not now vested. Of course, this figure includes large numbers of young, short-service workers who may obtain vested rights later on in their careers. But a disturbingly large number of older workers are not protected by vesting:

--40 per cent of plan participants age 45 or more are not vested;

--35 per cent of plan participants age 50 or more are not vested;

--26 per cent of plan participants age 55 or more are not vested.

Pensions, by their very nature, are of greatest concern to the older worker. Accordingly, this lack of vested rights for older workers is critical, for they experience the greatest hardships when benefit losses occur, and an older workers who loses benefit rights has far less opportunity to obtain a pension from a subsequent employer than does a younger worker.

While there is a need for some vesting--especially among older workers--it must be reecognized that a Federally-established vesting standard would raise costs for those plans without vesting and for those currently offering slow vesting. If these increased costs were excessive or ill-constructed, vesting could come at the expense of reduced future benefit payments for retirees and could discourage new or improved pension plans. For these reasons a "Rule of 50" was selected as a minimum standard; one which would be moderate in cost but which would bring rapid vesting for middle-aged and older workers.

The Rule of 50 would require 50 per cent vesting whenever any combination of age and years of plan participation equals 50, with vesting of an additional 10 per cent each year for five years thereafter. Thus, a worker who begins to participate in a plan at age 30 would, at age 40 with 10 years of covered service, become 50 per cent vested; a worker, age 45 with 5 years of covered service, would also achieve 50 per cent vesting. Both would be 100 per cent vested after 5 additional years.

To alleviate any danger that the Rule of 50 might limit new employment opportunities for older workers and also to keep vesting costs to a minimum, the Administration bill would allow plans to exclude employees from coverage until they have up to three years of service and/or attain a specified age not to exceed age 30. Also, plans could exclude an employee who first becomes eligible when he has attained an age which is within 5 years of the normal retirement age under the plan. In addition, to ease the impact of increased costs, only benefits accrued after a specified effective date would have to be vested under the minimum standard.

These vesting and eligibility standards would be written into the Internal Revenue Code and plans would have to adhere to them to maintain their tax-qualified status. It is for this reason that the

(more)

Administration bill would be administered by the Treasury Department, which has the expertise necessary for this particular job. In this regard, the President's proposal would not disturb the primary and appropriate role of the Treasury Department as the Federal agency administering matters related to the tax qualification of private pension plans.

4. Pension funds should be administered according to Federal standards of fiduciary responsibility.

Some 125 billion dollars have been accumulated in private pension funds to pay retirement benefits in future years. Control of these funds is shared by employers, unions, banks, insurance companies, and other entities. Most of this vast sum of money is honestly and effectively managed. But over the years instances have come to light where pension funds have been mismanaged, abused by self-dealing, or subjected to plain wrongdoing. Because the pension fund normally is the only security underlying benefit expectations other than the ability of contributing employers to continue in business, it is clear that plan participants should have sound protection against careless and corrupt fund management. To this end, the President asked Congress to enact the Employee Benefits Protection Act in March 1970, and again in his pension message of December 1971.

The EBPA would amend the existing Welfare and Pension Plans Disclosure Act in several significant ways. Most importantly, it would impose Federal standards of fiduciary responsibility on persons who control pension funds (and here I might add that the standards would apply also to managers of private employee welfare funds). These standards basically require that plan fiduciaries discharge their duties solely in the interests of plan participants and their beneficiaries, and that they do so in accordance with a "prudent man" role and the documents governing the fund. There are also some specific prohibitions against self-dealing and conflicts of interest. A fiduciary would be personally liable for losses caused by his breach of the standards, and plan participants in a class action or the Secretary of Labor could sue to recover the liability.

Other significant features of the EBPA (or "ficuciary bill," as it is popularly called) include broadened reporting and disclosure requirements, stronger investigatory and enforcement powers for the Secretary of Labor, and a prohibition against persons convicted of certain crimes from holding responsible positions in a plan. I should note, however, that the bill would not interfere with State laws which now regulate the insurance, banking and securities fields.

5. The Departments of Labor and the Treasury are undertaking a one-year study to determine the extent of benefit losses which result from plan terminations.

When a pension plan is terminated, an employee participating

(more)

in it can lose all or a part of the benefits which he has long been relying on, even if his benefits are fully vested. The extent to which terminations occur, the number of workers who are affected, and the degree to which they are harmed are questions about which we now have insufficient information. This information is needed in order to determine what Federal policy should be on questions such as funding, the nature of the employer's liability, and termination insurance.

The wrong solution to the terminations problem could do more harm than good by raising unduly the cost of pension plans for the many workers who are not affected by terminations. It is important, therefore, that the nature and scope of this problem be carefully and thoroughly investigated. To this end, the President directed the Departments of Labor and the Treasury to complete their data collection plan on terminations by the close of 1972.

That concludes my description of the five points which comprise the President's program on pensions. Now I would not be candid if I left you with the impression that no other pension proposals have come to the attention of Congress, or that there is not any controversy about what or how much should be done. Quite the reverse is true, and it would take much more time to describe the other proposals and compare them with the President's. Instead of doing that, let me leave with you a general characterization of the President's program. Basically, it regards private pension plans as valuable assets in our free enterprise system and seeks not to discourage their further growth and development. Some improvements--vesting and fiduciary standards--clearly are needed to make retirement expectations more secure. At the same time, the inequities that exist between the covered workers and the non-covered or inadequately covered can be remedied without the Federal Government redesigning the private retirement structure. Finally, the program does not attempt to experiment with ideas where basic data is needed.

Thank you for your attention. I would not be surprised if you now feel that I came here to sell you something--well-considered, practical pension proposals.

# # #

A.M. FRIDAY, OCT. 27, 1972
REGIONAL SEMINAR, AMERICAN INSURANCE MANAGEMENT INSTITUTE, COLUMBUS, OHIO

It is indeed a pleasure to speak here today. Insurance is a fascinating field and also a very technical one. It's something every layman like myself needs to have some knowledge of, and yet it's difficult for me to get among pro's on the subject without fearing that I will be talked into buying something. Well, I don't have to worry about that today. All of us here are on the consumer side of the insurance business--only I'm sure you are much sharper at it than I am. Indeed, your organization must be one of the oldest consumer interest groups in the country.

[redacted] I want to be careful that I don't lead you astray on what I came here to speak about. I didn't come here to speak about insurance--as you deal with it in your work--or to speak about [redacted] consumerism--as we hear so much about it in the avant garde movement of today. I'm here to talk about private employee pension benefit plans. [redacted] The debate on pension plans involves some ideas akin to insurance, some akin to consumerism, and some which emanate from the interests and prerogatives of management. So I wouldn't be surprised if many of you are [redacted] already familiar with the pension issues. But let me add a few more ideas that are involved in the pension controversy. They include equity in the workplace, income adequacy of older Americans, federal income tax, capital formation and concentration, and, as with [redacted] many important domestic issues of [redacted] today, the proper role of government regulation vis-a-vis the private decision-making process. In fact, there is hardly a domestic economic issue today which cannot be related in some way to our private pension system.

There are so many facets [redacted] of the pension controversy and the pension plans themselves are so various and technically complicated that one could go on for hours simply describing the context of the issues. But I won't do that here because I think you already must have a good general knowledge of the subject. In the last year or so there have been many magazine and newspaper articles and at least two television "specials" devoted to the problems of the private pension system. What I would like to do in the brief time available here is to describe the President's program on pensions and the [redacted] features of the two Administration bills which I introduced in the House of Representatives during the 92nd Congress.

Last December 8, President Nixon outlined his pension program in a message he sent to Congress. It is a five-point program which includes three new legislative proposals, a renewed endorsement of an earlier proposal, and a major study project which will provide the data needed to determine whether additional legislation should be recommended. Here are the essentials of the five points:

1. <u>Employees who wish to save independently for their retirement or to supplement employer-financed pensions should be allowed to deduct on their income tax returns amounts set aside for these purposes.</u>

Today only 30 million employees are covered by private retirement plans. Now I consider this fact--that about half of the private workforce has such coverage--to be a significant achievement and not at all a shortcoming. Nevertheless, the non-covered and independently covered workers should be encouraged to build up greater savings for retirement.

Under present law, both the contributions which an <u>employer</u> makes to a qualified private retirement plan on behalf of his employees and the investment earnings on those contributions are generally not subject to taxes until they are paid to the employee or to his beneficiaries. The tax liability on investment earnings is also deferred when an <u>employee</u> contributes to a group plan, though in this case the contribution itself is taxable. But when an employee saves independently for his own retirement, both his contribution and the investment earnings on such savings are currently subject to taxes.

This inequity discourages individual self-reliance and slows the growth of private retirement savings. It places an unfair burden on those employees (especially older workers) who want to establish a pension plan or augment an employer-financed plan. To provide such persons with the same opportunities now available to others, the Administration bill would make contributions to retirement savings programs by individuals deductible up to the level of $1500 per year or 20% of income, whichever is less. Individuals would retain the power to control the investment of these funds, channeling them into bank accounts, mutual funds, annuity or insurance programs, government bonds, or into other investments as they desire. Taxes would also be deferred on the earnings from these investments.

This provision would be especially helpful to older workers who are most interested in retirement. The limitation on deductions would direct benefits primarily to employees with low and moderate incomes, while preserving an incentive to establish employer-financed plans. The limit is nevertheless sufficiently high to permit older employees to finance a substantial retirement income. For example, a person whose plan begins at age 40, with contributions of $1500 a year, could still retire at age 65 with an annual pension of $7500, in addition to social security benefits.

This proposed deduction would be available to those already covered by employer-financed plans, but in this case the upper limit of $1500 would be reduced to reflect pension plan contributions made by the employer. An appropriate adjustment would also be made in the case of individuals who do not contribute to the Social Security system or the Railroad Retirement System.

2. <u>Self-employed persons who invest in pension plans for themselves and their employees should be given a more generous tax deduction than they now receive.</u>

Under present law, self-employed persons may establish pension plans covering themselves and their employees. However, deductible contributions are limited annually to $2500 or 10 percent of earned income, whichever is less. There are no such limits to contributions made by corporations on behalf of their employees.

This distinction in treatment is not based on any difference in reality, since self-employed persons and corporate employees often engage in substantially the same economic activities. One result of this distinction has been to create an artificial incentive for the self-employed to incorporate; another result has been to deny benefits to the employees of those self-employed persons who do not wish to incorporate which are comparable to those of corporate employees.

To achieve greater equity, the Administration bill would raise the annual limit for deductible contributions by the self-employed to $7500 or 15 percent of income, whichever is less. This provision would encourage and enable the self-employed to provide more adequate benefits for themselves and for their workers.

3. <u>A minimum standard should be established for the vesting of pensions.</u>

Inadequate vesting in pension plans is perhaps the most serious problem in our private pension system. Conceptually, vesting means that the benefit rights accrued by a plan participant will not be forfeited, even if he changes jobs or stops working before normal retirement age. When 10, 15, or 20 years of accrued pension credits suddenly go down the drain because of a layoff, illness, or opportunity for a better job, it is no consolation to be told that you have lost nothing because you never gained a legal right to a pension. The plain fact today is that, for the vast majority of plan participants, pension expectations are built up by going to work day in and day out, and not by hiring a lawyer and maybe also an actuary to advise you from time to time about your status under the plan's provisions.

More than two-thirds of all private pension plan participants are not now vested. Of course, this figure includes large numbers of oung, short-service workers who may obtain vested rights later on in their careers. But a disturbingly large number of older workers are not protected by vesting:

--40 percent of plan participants age 45 or more are not vested;

--35 percent of plan participants age 50 or more are not vested;

--26 percent of plan participants age 55 or more are not vested.

Pensions, by their very nature, are of greatest concern to the older worker. Accordingly, this lack of vested rights for older workers is critical, for they experience the greatest hardships when benefit losses occur, and an older worker who loses benefit rights has far less opportunity to obtain a pension from a subsequent employer than does a younger worker.

While there is a need for some vesting--especially among older workers--it must be recognized that a Federally-established vesting standard would raise costs for those plans without vesting and for those currently offering slow vesting. If these increased costs were excessive or ill-constructed, vesting could come at the expense of reduced future benefit payments for retirees and could discourage new or [redacted] improved pension plans. For these reasons a "Rule of 50" was selected as a minimum standard; one which would be moderate in cost but which would bring rapid vesting for middle-aged and older workers.

The Rule of 50 requires 50 percent vesting whenever any combination of age and years of plan participation equals 50, with vesting of an additional 10 percent each year for five years thereafter. Thus, a worker who begins to participate in a plan at age 30 would, at age 40 with 10 years of covered service, become 50 percent vested; a worker, age 45 with 5 years of covered service, would also achieve 50 percent vesting. Both would be 100 percent vested after 5 additional years.

To alleviate any danger than the Rule of 50 might limit new employment opportunities for older workers and also to keep vesting costs to a minimum, the Administration bill would allow plans to [redacted] exclude employees from coverage until they have up to three years of service and/or attain a specified age not to exceed age 30. Also, plans could exclude an employee who first becomes eligible when he has attained an age which is within 5 years of the normal retirement age under the plan. In addition, to ease the impact of increased costs, only benefits accrued after a specified effective date would have to be vested under the minimum standard.

These vesting and eligibility standards would be written into the Internal Revenue Code and plans would have to adhere to them to maintain their tax-qualified status. It is for this reason that the Administration bill would be administered by the Treasury Department, which has the expertise necessary for this particular job. In this regard, the President's proposal would not disturb the primary and appropriate role of the Treasury Department as the Federal agency administering matters related to the tax qualification of private pension plans.

4. <u>Pension funds should be administered according to Federal standards of fiduciary responsibility.</u>

Some 125 billion dollars have been accumulated in private pension funds to pay retirement benefits in future years. Control of these funds is shared by employers, unions, banks, insurance companies, and other entities. Most of this vast sum of money is honestly and effectively managed. But over the years instances have come to light where pension funds have been mismanaged, abused by self-dealing, or subjected to plain wrongdoing. Because the pension fund normally is the only security underlying benefit expectations other than the ability of contributing employers to continue in business, it is clear that plan participants should have sound protection against careless and corrupt fund management. To this end, the President asked Congress to enact the Employee Benefits Protection Act in March 1970, and again in his pension message of December 1971.

The EBPA would amend the existing Welfare and Pension Plans Disclosure Act in several significant ways. Most importantly, it would impose Federal standards of [redacted] fiduciary responsibility on persons who control pension funds (and here I might add that the standards would apply also to managers of private employee welfare funds). These standards basically require that plan fiduciaries discharge their duties solely in the interests of plan participants and their beneficiaries, and that they do so in accordance with a "prudent man" rule and the documents governing the fund. There are also some specific prohibitions against self-dealing and conflicts of interest. A fiduciary would be personally liable for losses caused by his breach of the standards, and plan participants in a class action [redacted] or the Secretary of Labor could sue to recover the liability.

Other significant features of the EBPA (or "fiduciary bill," as it is popularly called) include broadened reporting and disclosure requirements, stronger investigatory and enforcement powers for the Secretary of Labor, and a prohibition against persons convicted of certain crimes from holding responsible positions in a plan. I should note, however, that the bill would not interfere with State laws which now regulate the insurance, banking and securities fields.

5. <u>The Departments of Labor and the Treasury are undertaking a one-year study to determine the extent of benefit losses</u> which result [redacted]

[redacted] from plan terminations.

When a pension plan is terminated, an employee participating in it can lose all or a part of the benefits which he has long been relying on, even if his benefits are [redacted] fully vested. The extent to which terminations occur, the number of workers who are affected, and the degree to which they are harmed are questions about which we now have insufficient information.

This information is needed in order to determine what Federal policy should be on questions such as funding, the nature of the employer's liability, and termination insurance.

The wrong solution to the terminations problem could do more harm than good by raising unduly the cost of pension plans for the many workers who are not affected by terminations. It is important, therefore, that the nature and scope of this problem be carefully and thoroughly investigated. [redacted] To this end, the President directed the Departments of Labor and the Treasury to complete their [redacted] data collection on plan [redacted] terminations by the close of 1972.

That concludes my description of the five points which comprise the President's program on pensions. Now I would not be candid if I left you with the impression that no other pension proposals have come to the attention of Congress, or that there is not any controversy about what or how much should be done. Quite the reverse is true, and it would take much more time to describe the other proposals and compare them with the President's. Instead of doing that, let me leave with you a general characterization of the President's program. Basically, it regards private pension plans as valuable assets in our free enterprise [redacted] system and seeks not to discourage their further growth and development. Some improvements -- vesting and fiduciary standards -- clearly are needed to make retirement expectations more secure. At the same time, the inequities that exist between the covered workers and the non-covered or inadequately covered can be remedied without the Federal Government redesigning the private retirement structure. Finally, the program does not attempt to experiment with ideas where basic data is needed.

Thank you for your attention. I would not be surprised if you now feel that I came here to sell you something -- well-considered, practical pension proposals.

A Office Copy

REMARKS BY REP. GERALD R. FORD, R-MICH.
REPUBLICAN LEADER, U. S. HOUSE OF REPRESENTATIVES
BEFORE THE AMERICAN INSURANCE MANAGEMENT INSTITUTE
REGIONAL SEMINAR
COLUMBUS, OHIO
FRIDAY MORNING, OCTOBER 27, 1972

It is indeed a pleasure to speak here today. Insurance is a fascinating field and also a very technical one. It's something every layman like myself needs to have some knowledge of, and yet it's difficult for me to get among pro's on the subject without fearing that I will be talked into buying something. Well, I don't have to worry about that today. All of us here are on the consumer side of the insurance business--only I'm sure you are much sharper at it than I am. Indeed, your organization must be one of the oldest consumer interest groups in the country.

I want to be careful that I don't lead you astray on what I came here to speak about. I didn't come here to speak about insurance--as you deal with it in your work--or to speak about consumerism--as we hear so much about it in the avant garde movement of today. I'm here to talk about private employee pension benefit plans. The debate on pension plans involves some ideas akin to insurance, some akin to consumerism, and some which emanate from the interests and prerogatives of management. So I wouldn't be surprised if many of you are already familiar with the pension issues. But let me add a few more ideas that are involved in the pension controversy. They include equity in the workplace, income adequacy of older Americans, Federal income tax, capital formation and concentration, and, as with many important domestic issues of today, the proper role of government regulation vis-a-vis the private decision-making process. In fact, there is hardly a domestic economic issue today which cannot be related in some way to our private pension system.

There are so many facets of the pension controversy and the pension plans themselves are so various and technically complicated that one could go on for hours simply describing the context of the issues. But I won't do that here because I think you already must have a good general knowledge of the subject. In the last year or so there have been many magazine and newspaper articles and at least two television "specials" devoted to the problems of the private pension system. What I would like to do in the brief time available here is to describe the President's program on pensions and the features of the two Administration

(more)

bills--one of which I introduced in the House of Representatives during the 92nd Congress.

Last December 8, President Nixon outlined his pension program in a message he sent to Congress. It is a five-point program which includes three new legislative proposals, a renewed endorsement of an earlier proposal, and a major study project which will provide the data needed to determine whether additional legislation should be recommended. Here are the essentials of the five points:

1. Employees who wish to save independently for their retirement or to supplement employer-financed pensions should be allowed to deduct on their income tax returns amounts set aside for these purposes.

Today only 30 million employes are covered by private retirement plans. Now I consider this fact--that about half of the private workforce has such coverage--to be a significant achievement and not at all a shortcoming. Nevertheless, the non-covered and independently covered workers should be encouraged to build up greater savings for retirement.

Under present law, both the contributions which an employer makes to a qualified private retirement plan on behalf of his employees and the investment earnings on those contributions are generally not subject to taxes until they are paid to the employee or to his beneficiaries. The tax liability on investment earnings is also deferred when an employee contributes to a group plan, though in this case the contribution itself is taxable. But when an employee saves independently for his own retirement, both his contribution and the investment earnings on such savings are currently subject to taxes.

This inequity discourages individual self-reliance and slows the growth of private retirement savings. It places an unfair burden on those employees (especially older workers) who want to establish a pension plan or augment an employer-financed plan. To provide such persons with the same opportunities now available to others, the Administration bill would make contributions to retirement savings programs by individuals deductible up to the level of $1500 per year or 20 per cent of income, whichever is less. Individuals would retain the power to control the investment of these funds, channeling them into bank accounts, mutual funds, annuity or insurance programs, government bonds, or into other investments as they desire. Taxes would also be deferred on the earnings from these investments.

This provision would be especially helpful to older workers who are most interested in retirement. The limitation on deductions would direct benefits primarily to employees with low

(more)

and moderate incomes, while preserving an incentive to establish employer-financed plans. The limit is nevertheless sufficiently high to permit older employees to finance a substantial retirement income. For example, a person whose plan begins at age 40, with contributions of $1500 a year, could still retire at age 65 with an annual pension of $7500, in addition to social security benefits.

This proposed deduction would be available to those already covered by employer-financed plans, but in this case the upper limit of $1500 would be reduced to reflect pension plan contributions made by the employer. An appropriate adjustment would also be made in the case of individuals who do not contribute to the Social Security system or the Railroad Retirement System.

2. Self-employed persons who invest in pension plans for themselves and their employees should be given a more generous tax deduction than they now receive.

Under present law, self-employed persons may establish pension plans covering themselves and their employees. However, deductible contributions are limited annually to $2500 or 10 per cent of earned income, whichever is less. There are no such limits to contributions made by corporations on behalf of their employees.

This distinction in treatment is not based on any difference in reality, since self-employed persons and corporate employees often engage in substantially the same economic activities. One result of this distinction has been to create an artificial incentive for the self-employed to incorporate; another result has been to deny benefits to the employees of those self-employed persons who do not wish to incorporate which are comparable to those of corporate employees.

To achieve greater equity, the Administration bill would raise the annual limit for deductible contributions by the self-employed to $7500 or 15 per cent of income, whichever is less. This provision would encourage and enable the self-employed to provide more adequate benefits for themselves and for their workers.

3. A minimum standard should be established for the vesting of pensions.

Inadequate vesting in pension plans is perhaps the most serious problem in our private pension system. Conceptually, vesting means that the benefit rights accrued by a plan participant will not be forfeited, even if he changes jobs or stops working before normal retirement age. When 10, 15, or 20 years of accrued pension credits suddenly go down the drain because of a layoff, illness, or opportunity for a better job, it is no consolation to be told that you have lost nothing because you never gained a legal right to a pension. The plain fact today is that, for the vast majority of plan participants, pension expectations are built up by going to work day in and day out, and not by hiring a lawyer and maybe also an actuary

(more)

to advise you from time to time about your status under the plan's provisions.

More than two-thirds of all private pension plan participants are not now vested. Of course, this figure includes large numbers of young, short-service workers who may obtain vested rights later on in their careers. But a disturbingly large number of older workers are not protected by vesting:

--40 per cent of plan participants age 45 or more are not vested;

--35 per cent of plan participants age 50 or more are not vested;

--26 per cent of plan participants age 55 or more are not vested.

Pensions, by their very nature, are of greatest concern to the older worker. Accordingly, this lack of vested rights for older workers is critical, for they experience the greatest hardships when benefit losses occur, and an older workers who loses benefit rights has far less opportunity to obtain a pension from a subsequent employer than does a younger worker.

While there is a need for some vesting--especially among older workers--it must be recognized that a Federally-established vesting standard would raise costs for those plans without vesting and for those currently offering slow vesting. If these increased costs were excessive or ill-constructed, vesting could come at the expense of reduced future benefit payments for retirees and could discourage new or improved pension plans. For these reasons a "Rule of 50" was selected as a minimum standard; one which would be moderate in cost but which would bring rapid vesting for middle-aged and older workers.

The Rule of 50 would require 50 per cent vesting whenever any combination of age and years of plan participation equals 50, with vesting of an additional 10 per cent each year for five years thereafter. Thus, a worker who begins to participate in a plan at age 30 would, at age 40 with 10 years of covered service, become 50 per cent vested; a worker, age 45 with 5 years of covered service, would also achieve 50 per cent vesting. Both would be 100 per cent vested after 5 additional years.

To alleviate any danger that the Rule of 50 might limit new employment opportunities for older workers and also to keep vesting costs to a minimum, the Administration bill would allow plans to exclude employees from coverage until they have up to three years of service and/or attain a specified age not to exceed age 30. Also, plans could exclude an employee who first becomes eligible when he has attained an age which is within 5 years of the normal retirement age under the plan. In addition, to ease the impact of increased costs, only benefits accrued after a specified effective date would have to be vested under the minimum standard.

These vesting and eligibility standards would be written into the Internal Revenue Code and plans would have to adhere to them to maintain their tax-qualified status. It is for this reason that the

(more)

Administration bill would be administered by the Treasury Department, which has the expertise necessary for this particular job. In this regard, the President's proposal would not disturb the primary and appropriate role of the Treasury Department as the Federal agency administering matters related to the tax qualification of private pension plans.

4. <u>Pension funds should be administered according to Federal standards of fiduciary responsibility</u>.

Some 125 billion dollars have been accumulated in private pension funds to pay retirement benefits in future years. Control of these funds is shared by employers, unions, banks, insurance companies, and other entities. Most of this vast sum of money is honestly and effectively managed. But over the years instances have come to light where pension funds have been mismanaged, abused by self-dealing, or subjected to plain wrongdoing. Because the pension fund normally is the only security underlying benefit expectations other than the ability of contributing employers to continue in business, it is clear that plan participants should have sound protection against careless and corrupt fund management. To this end, the President asked Congress to enact the Employee Benefits Protection Act in March 1970, and again in his pension message of December 1971.

The EBPA would amend the existing Welfare and Pension Plans Disclosure Act in several significant ways. Most importantly, it would impose Federal standards of fiduciary responsibility on persons who control pension funds (and here I might add that the standards would apply also to managers of private employee welfare funds). These standards basically require that plan fiduciaries discharge their duties solely in the interests of plan participants and their beneficiaries, and that they do so in accordance with a "prudent man" role and the documents governing the fund. There are also some specific prohibitions against self-dealing and conflicts of interest. A fiduciary would be personally liable for losses caused by his breach of the standards, and plan participants in a class action or the Secretary of Labor could sue to recover the liability.

Other significant features of the EBPA (or "ficuciary bill," as it is popularly called) include broadened reporting and disclosure requirements, stronger investigatory and enforcement powers for the Secretary of Labor, and a prohibition against persons convicted of certain crimes from holding responsible positions in a plan. I should note, however, that the bill would not interfere with State laws which now regulate the insurance, banking and securities fields.

5. <u>The Departments of Labor and the Treasury are undertaking a one-year study to determine the extent of benefit losses which result from plan terminations</u>.

When a pension plan is terminated, an employee participating

(more)

in it can lose all or a part of the benefits which he has long been relying on, even if his benefits are fully vested. The extent to which terminations occur, the number of workers who are affected, and the degree to which they are harmed are questions about which we now have insufficient information. This information is needed in order to determine what Federal policy should be on questions such as funding, the nature of the employer's liability, and termination insurance.

The wrong solution to the terminations problem could do more harm than good by raising unduly the cost of pension plans for the many workers who are not affected by terminations. It is important, therefore, that the nature and scope of this problem be carefully and thoroughly investigated. To this end, the President directed the Departments of Labor and the Treasury to complete their data collection plan on terminations by the close of 1972.

That concludes my description of the five points which comprise the President's program on pensions. Now I would not be candid if I left you with the impression that no other pension proposals have come to the attention of Congress, or that there is not any controversy about what or how much should be done. Quite the reverse is true, and it would take much more time to describe the other proposals and compare them with the President's. Instead of doing that, let me leave with you a general characterization of the President's program. Basically, it regards private pension plans as valuable assets in our free enterprise system and seeks not to discourage their further growth and development. Some improvements--vesting and fiduciary standards--clearly are needed to make retirement expectations more secure. At the same time, the inequities that exist between the covered workers and the non-covered or inadequately covered can be remedied without the Federal Government redesigning the private retirement structure. Finally, the program does not attempt to experiment with ideas where basic data is needed.

Thank you for your attention. I would not be surprised if you now feel that I came here to sell you something--well-considered, practical pension proposals.

# # #