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ABSTRACT

Proceedings of a 1980 Brown University conference on faculty retirement are presented. Papers and authors are as follows: "A Review of Current Legal Status and National Policy Issues" (Laura C. Ford); "Mandatory Retirement Age Legislation for Tenured Faculty: The Policy Issues and Their Context" (W. Lee Hansen); "Retirement and Inflation: The Problem, Qualifications, and Some Modest Proposals for Change" (John H. Biggs); "The TIAA/CREF Perspective: The Unisex Issue" (Thomas C. Edwards); "TIAA/CREF and Planning for Retirement" (Donald S. Willard); "ADEA Implications for TIAA/CREF Retirement Plans" (John J. McCormack, Jr.); "Faculty: Planning for Retirement" (Aaron Lemonick); "COFHE Faculty Retirement Plans" (Janice Clinthorne); and "Financial Planning for Retirement" (George Barbee). Specific topics include: a federal legislative amendment to establish a general mandatory retirement at age 70 and the exemption provisions for tenured employees at postsecondary institutions; cessation of employer contributions to pension plans for post-retirement age employees; cases involving contract principles and the mandatory retirement of tenured faculty; public policy; and economic factors affecting individuals and postsecondary institutions. The comments of J. Russell Southworth and Robert F. Link are also included, along with questions and answers resulting from the conference sessions. (SW)

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FACULTY RETIREMENT

Proceedings from the
COFHE Retirement Conference

October 31 - November 1, 1980
Brown University
Providence, Rhode Island

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Consortium on Financing Higher Education
Cambridge, Massachusetts
1981

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Foreword

The purpose of this volume is to share with other institutions of higher education and the academic community at large the ideas and information generated at the 1980 COFHE Conference on Faculty Retirement. That conference which was, of necessity, limited to our membership, provided a logical follow-up to the reports* on our two year study of the impact of changes in the mandatory retirement age on faculty. Those reports raised a number of important questions and issues about the adequacy of current plans, changing faculty needs and attitudes and the possibilities for devising new plans on improving existing plans. The purpose of the conference was to take yet another step towards a better understanding of the issues ahead, to suggest that some improvements can be made now, and to identify those areas where more research and planning would be the most fruitful. We hope that you will find these proceedings useful, but more than that, provocative.

The conference and this volume would not exist without the continuing financial support and the encouragement from the Andrew Mellon Foundation, nor without the real contributions and enthusiastic support of the COFHE membership. We are grateful for both. But the work is not yet done. We must continue to seek new approaches to retirement and to improve the opportunities and services available to the ultimate beneficiaries of our efforts — the staff and faculty of every institution of higher education.

* A series of four reports published in June, 1980 and available upon request, at cost, from COFHE.

FIRST SESSION

Presiding:

Katharine H. Hanson
Executive Director
Consortium on Financing Higher Education

Introduction:

Colin Campbell
Chairman, COFHE Retirement Study
Advisory Committee
President, Wesleyan University

"A Review of Current Legal Status and National Policy Issues"

Speakers:

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W. Lee Hansen
Professor of Economics
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Moderator:

J. Russell Southworth
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Introduction

Colin G. Campbell

Colin Campbell is President of Wesleyan University. He is a past Chairman of the COFHE Board of Directors and is now Chairman of the COFHE Retirement Study Advisory Group.

* * * *

Welcome to the COFHE Retirement Conference. We are very pleased to be here at Brown University. I for one, having lived with this issue now pretty actively for the last couple of years, am absolutely delighted by the turnout here today, not only in terms of the numbers and quality, but in terms of the range of perspectives that this group represents in terms of faculty members, academic administrators, persons from other aspects of university and college administration like presidents, financial officers, personnel officers. It's the kind of mix that we had hoped would occur, and we are very pleased to see that it has. I do want to introduce on my right here our presiding officer for this conference, Kay Hanson; you'll be hearing from her in just a few moments, but it should be quite clear that Kay has played a leading role in the study which has brought us to this conference and we're all very grateful to her for the work that she has done. I'm also delighted to welcome back from the West Coast for the weekend Eve Pratt Hoar who worked almost completely with this project while she was a member of the COFHE staff last year.

I'd like to go back for a moment to how we got here to give you a little bit of perspective before we get on to the substantive discussion of the day. In May of 1978 the Consortium submitted a proposal to the Andrew Mellon Foundation for

support of a project which was really quite different from those previously undertaken by this organization. While all of us who were then on the Board of COFHE were well aware of the Consortium's limited financial resources and the demands on its staff, we were also deeply concerned about the implications of the Age Discrimination in Employment Act of 1978 as it related to the academic community. Already troubled by the pressures of inflation on our institutional budgets and on the value of the retirement funds of our faculty members, we sensed as a group, but we weren't in a position to document with sufficient specficity, that provisions of the legislation concerning mandatory retirement were likely to exacerbate the difficulties already anticipated for the 1980's. The Board concluded that a major effort was required to gain a better understanding of the impact of prohibiting mandatory retirement until age 70. Among our concerns were the obvious ones -- you've all shared them -- relating to the hiring of young faculty, affirmative action, tenure ratios, fringe benefit policies. We felt uninformed about faculty attitudes toward their employment and toward retirement, about early retirement programs available on our campuses, and about untried options to relieve the pressures which were bound to build. We believed that there was an information void and that policy issues of great importance might well remain unstudied unless the Consortium determined to plan an active role.

Very fortunately, the President of the Andrew W. Mellon Foundation, Jack Sawyer, who is with us today, not only shared our concerns, but sensed that a significant effort to address these issues was essential and urgent. I know I speak for all the COFHE institutions, and I suspect over time as the work of this study permeates out to other institutions, many others in higher education, in expressing gratitude to the Foundation and to Jack Sawyer for the interest and the support which got

this effort underway. It's a very valuable and significant public service. With the support of the Foundation we moved ahead, first forming an Advisory Committee of representatives from sixteen of our institutions and designing a study program, which is easy to say but took a long time, and finally retaining consultants to work with us. It took longer than any of us expected to determine exactly what the questions were, much less the answers. The shoddy state of the information concerning faculties on many of our campuses resulted in some further delays, because we were all in agreement on the Advisory Committee that the effort was important enough to require reliable and accurate data. When the reports of the consultants began to appear last year, first in draft for lengthy discussion, and then in final form, we realized as a group just how much we were learning about faculty profiles and attitudes and about the policies and planning underway on our various campuses.

You've all received the reports, and, I'm sure, read every word, and I won't take the time how to describe them or to summarize their conclusions. I gather and hope that you have found them interesting and useful. One of our goals over this weekend is to be sure that those reports are effectively used. They are full of information, valuable information; they are full of ideas, good ideas; and they deserve, I think, the most serious attention, not only from those of you who have come here this weekend, but also from many others on our campuses.

As the report phase of this project neared completion last spring, the Advisory Committee became convinced that a conference involving representatives from member institutions and a range of experts would be an appropriate and, in fact, a necessary next step. Enough questions about changing national policy and legal interpretations remained unanswered. Advice on how to use the data which had been painstakingly gathered

could be helpful to those developing and implementing institutional policies. Successful early retirement programs warranted study and discussion. New ideas about the nature and funding of retirement plans needed exposure. The crucial perspective of TIAA/CREF executives needed to be heard, and ways of responding to faculty concerns and of providing useful counseling had to be examined. And that's what this afternoon's program and tomorrow's program are about.

I do want to thank our speakers and our panelists for taking the time to be here and to share their thoughts and their ideas with the rest of us. I also want to urge that these be active participatory sessions starting this afternoon and running through tomorrow. It's very important, I think, that we all get our two cents in when we wish to, and we'll try to make every effort to make that possible. With the help of our panelists and our speakers, I think we ought to leave here better prepared to address one of the most significant issues facing our institutions, our faculties, and higher education.

It's going to be clear from these sessions that there are still some legal and policy issues requiring continuing attention, and I hope you will be thinking as we discuss this afternoon and tomorrow about areas in which you feel that the Consortium might be involved in the future in helping to address. The Board hasn't considered these questions, and I'm not even a member of it so I'm not going to volunteer that it will decide to do so; but I do think that it makes sense to take some time to think about a future role, if any, for the Consortium. I think the Board would value that input from this group, and so I hope you will keep that question on your minds as we discuss the other issues on our agenda. With that, let me thank you again, all of you, for being here. I look forward to participating with you today and tomorrow.

A Review of Current Legal Status and National Policy Issues

Laura C. Ford

Ms. Ford is a graduate of Wake Forest and the University of Virginia Law School. She has practiced law in New Haven and served as the Assistant General Counsel of ACE. She is now at Princeton University as a university counsel and, concurrently, pursuing a doctorate in classics.

* * * *

I notice on the map of the Brown campus mailed to conference participants that The Faculty Club is located on Benevolent Street, just off Benefit Street. Surely this demonstrates extraordinary perspicacity on Kay Hanson's part, as tomorrow's session in particular will consider the quandary of faculty members--who are anxious about the relative amounts of the two they will receive from their institutions upon retirement in an era of ravaging inflation.

This afternoon my assignment is to review the current legal status of mandatory retirement, and related national policy issues. In so doing, I am mindful not only that most of you are not lawyers, but also that many of you probably harbor deep-seated hostility towards the legal profession. I am reminded of the story about the social scientist who was conducting a survey to demonstrate how people in different vocations and professions often view the same problem quite differently. The researcher first approached an accountant and asked: "How much is two plus two?" The accountant replied that, under accounting principles with a commonly accepted margin of error, the sum of two and two can be anywhere between 3.99 and 4.01. The same question was then put to a mathematics

professor, who responded that the answer would depend upon the numberbase of your system; under our number system the answer is four, while under a system based on three, two plus two equals eleven. The researcher then approached a lawyer and said, "Counsellor, can you tell me how much is two plus two?" The lawyer paused and thought for a minute and said, "How much do you want it to be?" Indeed, we lawyers do not enjoy the highest public esteem, and I am afraid that my talk this afternoon may serve to reinforce rather than to dispel this notion.

The fall of 1977 and spring of 1978 witnessed a flurry of lobbying activity by the higher education community that was probably unprecedented in its intensity. The cause was amendment by Congress of the Age Discrimination in Employment Act of 1967 to establish a general mandatory retirement age of seventy; the result was a 3 1/2 year temporary exemption for tenured employees at postsecondary institutions. The wisdom and the efficacy of the exemption were widely questioned at the time, and predictions were made that the measure would inevitably foster litigation. In floor debates, for example, Congressman Floyd Fithian stated, "I feel strongly that the exemption provisions are unfair and will be challenged in court." Senator Church said, ". . . .the exemption is likely to be the source of much litigation or confusion." Yet the predicted law suits have not come to pass. October 1 of this year marked the exact midpoint of the 3 1/2 years, and to date only one case has been reported in the federal courts challenging the exemption (and that, as we shall see, was inconclusive).

As the recently-concluded COFHE study well demonstrates, the skills and expertise that must be garnered to cope with retirement-related issues are primarily those of labor economists, personnel specialists, and academic and financial planners.

Nevertheless, I will seek to bring you up to date on some of the still unresolved legal and political problems surrounding faculty retirement. Given the COFHE constituency, I will focus exclusively on private institutions.

As alluded to above, there has been one reported challenge to the tenured employee exemption in the ADEA Amendments of 1978. In Karlen v. New York University (S.D.N.Y., Feb. 1, 1979), a former tenured professor at N.Y.U. Law School, who had been mandatorily retired at age 65 before the effective date of the ADEA Amendments, made two claims: first, he claimed (for reasons that I will discuss later) that N.Y.U. violated the terms of its tenure contract with him when the university reduced its mandatory retirement age from 68 to 65; secondly, he claimed that--had he been allowed to stay on until age 68 as he was entitled to--he would have still been a tenured professor after the effective date of the ADEA Amendments, and therefore should have standing to challenge the constitutionality of the exemption. The court rejected his claim to standing, stating that there were far too many contingencies which made adjudication of the issue inappropriate (especially at the early stage of the litigation, which was on a pretrial motion to dismiss).

While the court's published opinion does not reveal the nature of the argument Karlen would have made against the constitutionality of the exemption, presumably his argument would have been that Congress had violated tenured employees right to equal protection of the laws under the due process clause of the Fifth Amendment. The appropriate legal test in such cases is whether a classification made by Congress is reasonably related to furthering a legitimate Government interest. My own opinion all along has been that the exemption is reasonably related to furthering a legitimate Government interest under the general rubric of

the health and well-being of American higher education. This interest can be more specifically stated in a number of ways, largely tracking the policy arguments made by many higher education representatives during the lobbying effort on the ADEA amendments. I understand that the legal ~~staff in the national office of the A.A.U.P. (which opposed enactment of the exemption) shares~~ this opinion and has actively discouraged several of its members from mounting legal challenges to the constitutionality of the exemption.

Assuming, then, that the exemption is with us to stay until July 1, 1982, my next point is to bring to your attention the rules ultimately decided upon to govern operation of the expiration date of the exemption. As you may recall, in the version of the implementing regulations originally proposed by the Department of Labor, age seventy was to be the applicable retirement age for tenured faculty with whom an employment relationship exists on and after July 1, 1982. Receipt of salary and benefits was to constitute conclusive proof of the existence of an employment relationship. Thus, in order for a tenured faculty member to be retired at the end of the 1981-82 academic year, all salary and benefits would have had to cease on or before June 30, 1982. As a result of arguments made by A.C.E. and the other associations that some institutions' fiscal years--and thus salary and benefits-- extend through July and August, the final regulations issued by the E.E.O.C. adopted a different standard. Section 1625.11 of the regulations states, "Individuals who attain age 65 prior to July 1, 1982 and all of whose job duties and responsibilities cease prior to that date will not be considered outside the exemption merely because their contract (or similar arrangement) providing for unlimited tenure expires on or after July 1, 1982."

And what will happen when the exemption expires? Is the higher education community reconciled to living with a retirement age of seventy, or will it seek to have the exemption made permanent? And if such efforts are made, what will be the likelihood of success?

Obviously, one would need a crystal ball to answer these questions. The makeup of the 97th Congress is as yet unknown. Also, neither the interim study (due January 1, 1981) nor the final study (due January 1, 1982) of the exemption's effects has been completed by the Department of Labor for submission to Congress. (We might learn more about the progress of these studies from our next speaker--W. Lee Hanson.) Whatever the study results, one cannot escape from the fact that the exemption was a desperate last-ditch measure to buy time that was highly unpopular from the beginning. Also, the political thrust is clearly in the opposite direction, i.e. towards the elimination of mandatory retirement altogether. Several bills to that effect were introduced in the 96th Congress, including Congressman Claude Pepper's HR 70 (to uncap the ADEA and eliminate all exemptions) and another bill to add age to the impermissible bases of discrimination in Title VII of the Civil Rights Act of 1964. According to the staff of the House Select Committee on Aging with whom I spoke earlier this week, there is no doubt that the upcoming Congress will give attention to the general issue of mandatory retirement.

To sum up, all that one can say is that, while there is no immediate danger, the gradual aging of the American population and continuing inflationary pressures make it likely that the "uncapping" monster will rear its ugly head in the not too distant future. When it does, the higher education community had better have its facts and figures ready, and certainly the COFHE project is a good first step.

Leaving the exemption now, I would like to focus upon a conceptually and legally separate matter, the question of cessation of employer contributions to pension plans for employees who continue working beyond the normal retirement age. The operative section of the ADEA prohibits discrimination on the basis of age in all terms and conditions of employment, and on its face would appear to prohibit such cessation (in the absence of a statutory exception). However, the legislative history of the 1978 amendments--including the Senate committee report and explicit statements in the floor debates in both houses--makes as clear as possible that the majority and minority managers of the bill had the view that cessation would be permitted. Thus, you have all the makings of a legal dilemma, and a situation in which a court would write a well-reasoned, definitive opinion either way--depending upon whether it invokes the principle that legislative history may be used to interpret but not to vary the plain meaning of the words of a statute, or the competing principle that the intention of Congress must be effectuated regardless of problems with wording.

In addition, as a further complication, confusion has persisted over whether cessation of contributions violates the Employee Retirement Income Security Act. The prevailing view has been that ERISA neither requires nor prohibits continued contributions after an employee reaches normal retirement age. This was the Department of Labor's view at the time of hearings on the ADEA Amendments, and in November of 1979 the I.R.S. issued a private ruling to the same effect. (Labor and Treasury share authority for enforcement of E.R.I.S.A.).

Despite internal divisions, the Department of Labor issued a final interpretation on this and other employee benefit questions on May 25, 1979, concluding that employers with nonsupplemental

defined contribution plans may cease contributions on behalf of employees who continue working beyond the normal retirement age (and that employers with defined benefit plans may take analogous measures). On July 1, 1979, authority to enforce the ADEA shifted from the Department of Labor to the E.E.O.C., and it is well-known that the E.E.O.C. ~~has been unhappy with Labor's interpretation all~~ along. Almost immediately after assuming jurisdiction, the E.E.O.C.'s Staff Committee on Policy took up the issue and sought a means of prohibiting cessation of contributions that would be both legal and agreeable to all the agencies involved.

The obvious solution of simply requiring continuation of contributions to age seventy seemed inadequate to the E.E.O.C. staff, once they realized that employers would simply reduce their contributions so that employees' accumulations at the time of mandatory retirement would be no greater than they would have been at the time of normal retirement. For example, according to TIAA-CREF's figures, continuation of contributions to age seventy would result in a 50% increase in the average person's accumulation (to fund a retirement of five years' shorter duration). Institutions could aim at the present level of retirement benefits by making a 30% reduction in contributions. This would mean that people would have to work to age seventy (i.e., that they would effectively be deprived of a realistic option to retire at age sixty-five). The Congressional intent of personal choice with regard to retirement age would thus be thwarted.

The most recent draft of the E.E.O.C.'s proposals that I have seen introduces a new concept, that of "benefit goals." The proposals would require that contributions continue for employees whose individual accounts are not sufficient at normal retirement age to meet "the benefit goals specified in the plan" and for those participants

in plans for which no benefit goals are specified (usually profitsharing, thrift and savings plans as opposed to money purchase and target plans).

The problems with such an approach, both philosophical and technical, would obviously be monumental. What is a reasonable benefit goal? How about short-service, as compared with career, employees? What about the equity problem between TIAA and CREF? Wouldn't you really be blurring the distinction between defined contribution and defined benefit plans, in that the so-called "benefit goal" would become an implied benefit guarantee?

The fact that sixteen months have passed without formal E.E.O.C. action on the proposals may indicate some appreciation of the enormity of these and other complicating factors. Or it may simply indicate some post-Gilbert gun-shyness on the Commission's part. (An anonymous E.E.O.C. official was quoted in the Legal Times of Washington last October as having said that the E.E.O.C. might look foolish if it changed Labor's already established regulations; this represents some new sensitivity on their part.) In any event, according to Jay Pagano in the E.E.O.C.'s general counsel's office earlier this week, no action is scheduled by the Commission on the proposals in the near future.

Before I turn away from statutes and regulations and to contract law, I would remind you not to overlook your applicable state and municipal statutes and ordinances dealing with discrimination on the basis of age. Institutions in California and Connecticut have had especially disruptive encounters with their respective state legislatures on the retirement issue.

In addition to these multiple sources of legal obligation by enactment of legislative bodies,

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colleges and universities should be aware of another source of applicable law which has likewise been in ferment in recent years—the common law of contracts. At the time an institution awards tenure to a faculty member, it enters into a long-term employment contract with him or her, with mutual rights and obligations. Typically, the faculty member receives only a letter of appointment or reappointment each year, and the terms and conditions of employment (beyond the barebones of salary and relevant dates) are contained in faculty handbooks and other published materials. When a matter in dispute is not covered by any institutional documents, courts must look to the testimony of witnesses in quest of the mutual understanding of the contracting parties. And, as is often the case when matters of common understanding within the academic world are at issue, courts will look to sources outside a given institution for assistance.

Such has been the case in three recent retirement cases. The case of first impression was Rehor v. Case Western Reserve University, decided by the Supreme Court of Ohio in 1975. A tenured professor of English challenged Case Western's mandatory retirement age of sixty-five on the ground that he had been awarded tenure by Western Reserve University, which had a mandatory retirement age of seventy, prior to its merger with Case Institute. The court concluded that obviously all terms and conditions of employment in effect at the time tenure is awarded cannot be frozen for thirty or thirty-five years; otherwise an institution could not adapt to changed circumstances. It therefore held that the University reserved the discretion to change the retirement age applicable to tenured faculty. (Also, and perhaps inconsistently, the court held that the faculty member's signature accepting reappointment each year gave his consent to the change.) Of interest to us is the fact that the University succeeded in its

argument concerning its discretion to change the retirement age by referring to several A.A.U.P. statements, particularly the Statement of Principles on Academic Retirement and Insurance Plans, issued in 1950, which emphasized institutional flexibility. A dissenting judge made reference to the same statement, arguing that the University had not met its obligation to make reasonable transition provisions for those adversely affected by any change.

A second noteworthy case is Drans v. Providence College, ruled on twice by the Supreme Court of Rhode Island (most recently on February 1, 1980). In that case a professor of modern languages sued for a declaratory judgment that he was not subject to Providence College's mandatory retirement age of sixty-five because that policy had been instituted after he was awarded tenure. The court concluded that the professor's signature on annual reappointment forms did not constitute consent, but nevertheless ruled in favor of the College. Following the reasoning of the Case Western case and also relying on the A.A.U.P. statements, the Rhode Island court held that, as long as a mandatory retirement program is adopted by a college in good faith, the age chosen is reasonable, the policy is uniformly applied to all faculty members, and the essential function of tenure is not compromised, the concept of tenure will not preclude the imposition of a mandatory retirement policy. The court remanded the case in order for the trial court to resolve the question of whether the reasonable expectations "within the academic community" would indicate that the professor was eligible for special consideration upon reaching the age of retirement.

That's when things became interesting. On remand, the trial justice commented, "I do not know what academic community the Supreme Court was referring to. All that I know is that this is a

controversy between a professor and Providence College and no one else. What Boston University thinks or may do or what the A.A.U.P. thinks or may do is of no consequence in resolving this controversy." He went on to construe the Supreme Court's use of the phrase "within the academic community" as meaning solely the community within the bounds of the Providence College campus, and within this frame of construction concluded that the College's award to the professor of an additional year of teaching beyond the age of sixty-five was a reasonable transition provision.

Needless to say, the case was again appealed to the state Supreme Court which, referring to the Case Western decision as well as several non-retirement cases, stated: ". . .we were speaking in terms of what we are now calling a 'national academic community,' a phrase which encompasses within its reach all institutions of higher learning in the United States." The case was again remanded, and there will be no final resolution, as the plaintiff is now deceased.

The third recent case involving contract principles and the mandatory retirement of tenured faculty is Karlen v. N.Y.U., decided by the federal district court for the Southern District of New York on February 1, 1979, which I discussed at the beginning of this talk in connection with the constitutionality of the ADEA exemption. In that case a law professor challenged N.Y.U.'s reduction of its mandatory retirement age from sixty-eight to sixty-five. The court denied the University's motion to dismiss, holding that the professor's signature on reappointment letters did not constitute consent, and in so doing relied on the other cases I have discussed as well as on the AAUP statements.

You may be wondering by now why I have devoted so much time to this line of cases, in view of the

fact that the new federal law will effectively prevent institutions from reducing their retirement ages in the future. While that is true, there is an important underlying point concerning the role of A.A.U.P. statements in retirement cases (as well as in financial exigency cases such as Bloomfield College and Goucher College). It is of tremendous importance who articulates the commonly held understandings of the academic community concerning the terms and conditions of faculty employment, expecially in areas where the consensus of the past has eroded. Through vigilance and an aggressive posture in relevant litigation, the A.A.U.P. has gotten a firm foothold in the judicial door. It is up to institutional representatives, through their various associations, to be equally vigilant and to point out to courts where necessary, the difference between joint statements of the A.A.U.P. and institutional associations, on the one hand, and unilaterally issued A.A.U.P. statements on the other hand. A.C.E. fought this battle successfully in the Goucher College case, and I particularly commend to you an article on this issue in the Winter, 1978 edition of the Educational Record by W. Todd Furniss.

Finally, I would bring to your attention the 1980 revision of the 1950 Statement of Principles on Academic Retirement and Insurance Plans to which I referred earlier. This latest document was prepared by a joint committee of the A.A.U.P. and the Association of American Colleges, and appears in the September, 1980 edition of Academe. It is too long for me to summarize here, but I urge you to review it as part of your institution's retirement deliberations. If there are respects in which your institution's policies differ from those endorsed by the statement, for reasons that should be obvious by now I urge you to commit your policies to unambiguous writing. Otherwise, the A.A.U.P.'s policies may by judicial fiat be held to be your own.

Mandatory Retirement Age Legislation for Tenured Faculty The Policy Issues and Their Context

W. Lee Hansen

Dr. Hansen is a member of the Department of Economics of the University of Wisconson-Madison. A graduate of the University of Wisconsin and Johns Hopkins University, he has held a number of distinquished fellowships and has served as Senior Staff Economist for the President's Council of Economic Advisers.

He is currently codirecting a study of the impact of the change in mandatory retirement in the academic sector for the Department of Labor.

* * * *

My assignment today is to review the major policy issues and their context so as to set the stage for your discussion of retirement policies and programs at your institutions. All of this is occasioned by the impressive series of reports prepared by COFHE on the impact of changes in the age of mandatory retirement at its member institutions. My comments will touch on a variety of topics:

(1) the major public policy issues affecting retirement at colleges and universities as they are likely to unfold over the next few years;
(2) how the resolution of these issues will affect the range of opportunities open to your individual institutions;
(3) likely changes in the economic position of faculty members that will affect and influence their plans for retirement; and

(4) prospective developments in higher education finance over the 1980s.

The Major Policy Issues

Two overriding policy issues, plus another subsidiary but still important issue, confront us in dealing with retirement in higher education. ~~One is whether congress will decide to continue~~ the exemption for tenured faculty members from the provisions of the 1978 amendments to the Age Discrimination in Employment Act of 1967. In July 1982 the current exemption expires, meaning that the minimum mandatory retirement age for tenured faculty members will rise to age 70, unless state law authorizes a higher age or none at all. It is well-known that many state legislatures have moved rapidly to respond to the federal legislation by making a similar change and in some cases prohibiting altogether any mandatory age of retirement. Because of these changes, a continuation by the federal government of the present exemption would leave a considerably smaller fraction of all tenured faculty subject to retirement at age 65 than was the case prior to introduction of the federal legislation in 1977.

This raises the interesting and important question as to whether higher education should organize itself to fight to make the exemption a permanent one. How much support would come from faculty and administrators at colleges and universities across the country? What support would come from the higher education establishment in Washington? How strong would this support be if only a small segment of higher education were affected? I believe that continuation of the exemption would be a hard battle to fight and to win. But if there is to be a fight, the strategy for guiding it should be organized soon.

The second issue is how to react to frequently-made proposals that there be no minimum MRA whatsoever. Both presidential candidates favored this position. In the heat of a political campaign it is easy to make promises like this. At the same time I expect that for some months Representative Claude Pepper has been quietly plotting his strategy for uncapping the MRA. These signs suggest that retirement age will be a hot legislative issue in the very near future. If so, this raises the same question noted before: How should colleges and universities as a group deal with this proposal? Should they oppose it? On what basis? Should they argue for a permanent exemption at age 70, as a compromise with the present exemption? How do they make their case? What is so unique about higher education? Even if federal legislation exempts college faculty members, how can states be restrained from eliminating the exemption that the federal government finds quite acceptable? I leave these questions for you to ponder.

A third issue, still a bit further off, is a possible change in the age at which people are entitled to receive maximum social security benefits at retirement. Currently, that age is 65, with reduced benefits available at age 62. But even the condition of present and prospective social security financing, suggestions have already been made about changing the age at which maximum benefits are available, moving it from 65 to 67 or 68 and maybe even to age 70. Of course, this is a national question that transcends higher education. And yet if this change is made, it will have important consequences for the retirement of faculty members, particularly if the age 65 exemption should be made permanent; in any case, the average age of retirement could rise by several years as a result of a change like this.

Adjustments Within Higher Education

However these issues are resolved, this still leaves several important questions for colleges and universities—their faculties and administrators. Foremost in the minds of many is this question: How can retirement policies and programs be operated without excessive federal intrusion into the academic affairs of colleges and universities? The record of federal agencies in promulgating regulations designed to guide or govern implementation of the 1978 Amendments to the ADEA is reason enough to give anyone pause. The regulations have been slow in coming, they are extremely detailed, they are voluminous, and they tend to be less flexible than they could be.

On the assumption that the exemption does expire and the age of MRA goes to 70, then what? One option is simply to adapt, allowing faculty members to retire when they will. Many top-notch public institutions have long had a MRA of 70, and they seem to have flourished or at least survived over the years. Even though the teaching and research performances of some faculty members decline with age, knowledgeable faculty and administrators have coped with these problems in various ways. They have encouraged improved performance, reallocated responsibilities, suggested the possibility of early retirement, helped to work out early retirement arrangements, and in extreme cases and usually as a last resort, actually forced the reluctant to retire. One knowledgeable dean I know suggests that in his experience the real breaking point comes somewhere between age 65 and 70—with an earlier age 65 retirement forcing out many able faculty members prematurely and a later age 70 retirement creating problems for a small number of faculty whose performance has clearly deteriorated.

A second option--the one that concerns most of you here today--is to develop plans, policies, and programs to encourage earlier retirement. This will get rid of so-called "deadwood" and permit its replacement with new young faculty members whose presence will invigorate instruction and research. This means that early retirement programs must be designed that will benefit both the affected individuals and their institutions. Whether these voluntary programs will be effective in changing the quality of the faculty along the lines just suggested depends heavily on which faculty members are induced to retire. In other words, what kinds of early retirement incentives will be most helpful in stimulating selective early retirement? If these programs result in the early retirement of the now least able faculty members, then average quality will rise. But, if instead the ablest faculty members are attracted into early retirement, then everyone loses. This means that the incentives must be designed carefully to achieve institutional purposes.

An additional set of plans, policies, and programs will be necessary to deal with declines in the physical and intellectual vitality of aging faculty members. Institutions will no doubt be forced to devise procedures--not too elaborate we hope, but more formal than they now have--for periodically evaluating the performance of older faculty members and finding ways where necessary to retire some of them prematurely--for cause. This is not a pleasant task to contemplate. How are such decisions to be ~~made~~? What criteria will have to be employed to assess performance? Who will decide? The questions are numerous and difficult. And though we may somehow avoid this path, I am not too optimistic. In any case, we should begin to think about this now rather than later.

Dealing intelligently with these internal matters arising out of the resolution of the broad policy issues will be difficult. To the extent that the minimum age of MRA is raised, to say 70, at least some faculty members will take advantage of the change by continuing to teach. Others will continue to opt for early retirement, as has long been the case. On balance, however, the average age of retirements is likely to creep up by from one to three years, according to the best current estimates. Such estimates run counter to the finding that over the past two decades there has been a continuing decline in the average age of faculty retirements. Which of these two opposing forces will dominate--the trend toward earlier retirement or the possibility of continuing to teach until age 70?

New Pressures

It is clear that the economic pressures to defer retirement will heighten. One force pushing in that direction is inflation whose underlying rate is currently estimated to be about ten percent. This is up substantially from three percent a decade ago and from one percent twenty years ago. It is interesting to note the effect of inflation on retirement benefits. After five years at a one percent inflation rate the real value of a dollar of benefits drops by about six percent; at a three percent inflation rate it drops by about fifteen percent; at a ten percent inflation rate it drops by about forty percent, etc. To the extent that individual faculty members can see the effects of inflation on the real value of their benefits, and there is no reason to doubt this, they will opt to continue working. This will beef up the retirement annuities of those faculty members with defined contribution plans and augment the retirement benefits of those faculty under defined benefit plans.

While inflation is an important consideration, less attention has been given to the depressing fact that the starting real value of pension benefits has already been eroded by the declining real value of faculty salaries. Real faculty salaries fallen over the past decade, both absolutely and relative to other occupational groups. This means that pension accumulations have lagged seriously and this implies that the relative position of retired faculty members will be substantially reduced relative to a decade ago. The evidence on faculty salary declines is significant. Average salaries have fallen by almost 20 percent over the last decade, whether measured by rank, institutional category, or type of institution. This trend is likely to continue, with ever greater adverse consequences for faculty retirement benefits. The situation for faculty members contrasts sharply with the situation for other large groups of workers, those in federal, state and local governments, and in the unionized sectors of the private economy. Of course, the Social Security benefits received by most faculty members are indexed, thus lessening somewhat the impact of inflation. But this is small comfort since Social Security benefits are also indexed for all other retirees.

To sum up, faculty members will have to adjust to continuing inflation and declining real salaries, and as a result to reduced pension benefits. Their only means of adjustment is to defer retirement as long as possible.

If these problems are not enough, faculty members will also suffer disproportionately because of sharp recent and projected increases in the Social Security tax and wage base, as required by federal legislation passed several years ago. By the mid to late 1980s virtually all of the salaries of the vast majority of faculty members will be fully taxed under Social Security. And to

the extent that inflation continues to push faculty members into higher tax brackets (though perhaps more slowly than for most other groups), the after tax income of faculty members will rise much less sharply than their nominal incomes. Because of the way social security benefits are paid out, faculty members will gain relatively little from their additional payments. Nor will they see apparent gains in benefits accruing to them as a consequence of larger income tax payments. Thus, we find ourselves in a difficult situation. News of this will be unlikely to create joy among faculty members in the 1980s.

How strong is the likelihood that faculty salaries will continue their real absolute decline? Given the continuance of inflation and the improbability that faculty salaries will be indexed, inflation will continue to erode the real value of our salaries. Moreover, faculty salaries are unlikely to rise dramatically in nominal terms because of familiar constraints on the funds that provide salaries--legislative appropriations for public institutions and tuition plus fund raising efforts for private institutions. I do not have time to spell out my reasons for the expectation that faculty salaries will show no significant improvements. Nor is there time to dispel the popular notion that faculty salaries have lagged and will continue to lag because of the great abundance of new PhDs; this explanation ignores a variety of important institutional constraints.

Higher Education's Prospects

Let me now examine the prospects for higher education finance in the 1980s. The likelihood of seeing the funding base for higher education augmented is not great. Much depends on the state of the economy and on the amount of real economic growth we experience in the next ten years. This will determine the size of the total pie available

to individuals to allocate to meet their varying private and public needs.

The need for funds for higher education, and in turn their availability, will depend heavily at least in the public sector on enrollments. This is because enrollments determine total state aid which is cost per student multiplied by the number of students. Private institutions must rely on other sources of funds, including tuition and contributions. Here, too, however, total enrollment affects the amount of funds needed.

Partly for this reason the big uncertainity is over the direction and magnitude of enrollment changes. Economist Howard Bowen suggests that enrollments could rise substantially, and he suggests that they will, to the extent that we can cultivate and capture large untapped markets for our services. Economist Steven Dresch concludes that enrollments might drop by as much as 50 percent as potential students respond (by not enrolling) to the declining economic returns to college-going; they will opt in greater numbers than in the past not to attend college. The Carnegie Council on Public Policy suggests an intermediate position, with the likelihood of a 5-10 percent decline in enrollments. For individual institutions enrollment changes are likely to be greater, or smaller, whatever the overall change. They are also likely to be greater for the private than public sector institutions, given the tuition levels and differentials, institutional location, and the liberal arts orientation of many private colleges and universities.

Another source of uncertainty is the extent to which higher education will be saddled with new social mandates that will affect the demand for higher education and perhaps even more importantly the costs of higher education. One of these mandates is almost certain to be a greater push for

accountability, with consequent rules, costly reporting systems, need for specialized personnel to deal with them, etc. Increased amounts of remedial instruction are now being offered: whether we are being pushed to do this or pulled by our own choices is not entirely clear. By contrast, there could also be a new push for instructional support and special programs for research and for advanced training from the federal government. We may have seen the first stirrings of a new effort to promote such programs with the release in early October of a report to the President from the National Science Foundation and Department of Education on our lagging scientific and engineering education. What is important to recognize is the following. Some of these mandates we can do well, whereas others we are ill-equipped to provide. I expect that we will continue to seek to do those that we believe we can do well—in the areas of research and traditional instruction—and that we will lag in our efforts to do other things thrust upon us unwillingly.

What about the different sources of funds? There are five major sources of funds: students; their parents; state and private sources which provide the bulk of instructional funds; and the federal government. Student funding programs continue to evolve, but they have been given shape for the next five years by congressional action just a month ago. The reauthorization calls for a scheduled pattern of increases in student financial aid that we hope will be stable and predictable.

State support for public institutions and frequently for students attending private institutions is more difficult to predict, in large part because of public concern about the growth of government spending. The push for tax-expenditure limitation programs through constitutional amendments and legislative actions in the various

states could strike a serious blow against higher education. Witness the predicted consequences of the TISCH amendment in Michigan. Or take a state such as Wisconsin which has always been exceedingly generous in its support of higher education. Because of a tight state budget, we recently added a $30 per semester tuition surcharge at Madison. This may well mark a change in the decade-old formula that set tuition at 25 percent of instructional costs; prior to that it was 20 percent. When this is combined with the indexing of state income tax brackets in Wisconsin, which came as part of an almost $1 billion tax reduction a year ago, the state tax system will no longer be the money producer it has been in the past. To the extent that more funds are to be allocated to higher education they will have to be taken out of other programs. Whether we can build an effective case for added funding, against such programs as, say, welfare aid, is not all certain.

Private funding for higher education may suffer similarly. People may give less for the same reasons that underlie the anti-tax anti-expenditure sentiment. On the other hand, aggressive fund raising efforts by private institutions can put them in an especially strong position to compete with the public sector with respect to faculty salaries, early retirement programs, and the like. Perhaps they can also narrow the public-private tuition differential. This may be the long awaited ray of hope for private higher education.

Federal funding beyond student aid is also uncertain. Whether additional funding will be available for research remains to be seen. However, growing concern about slow productivity growth could well generate a new burst of enthusiasm for basic research, much of which would have to be done at the colleges and universities. How favorably inclined the federal government may be

to fund special programs designed to provide alternative support for top-notch young scholars to develop their research potential (in a period when academic jobs are not available for them) is also uncertain. Help of this kind can be critical in dealing with the shortrun problems arising from the change in the age of mandatory retirement and with the longrun problems arising, from the peculiar age structure of academe as we move into the 1980s.

Summary and Conclusions

Let me now summarize. The immediate policy issues concern the exemption which expires in 1982, and likely congressional action to eliminate all MRA. What should we do to affect this legislation? How will we adjust to this legislation, assuming it takes its predicted course? How can we work to minimize its adverse impact on the quality of American higher education?

Dealing with these questions is difficult for several reasons. First, inflation, which is likely to continue unabated, quickly erodes faculty salary increases and pushes more faculty members to continue teaching until they are forced to retire. Inflation also erodes the real and relative value of their hard-earned pension benefits. The continued increases in Social Security taxes and personal income taxes will contribute to further faculty disillusionment with their economic position. How they will cope with this is difficult to speculate about.

The prospects for higher education finance are not especially optimistic. State funding is likely to constrain public institutions in many ways and to prevent them from taking significant steps either to maintain real salaries or to stimulate earlier retirement. The private sector, though hard pressed, will have greater flexibility

to deal with early retirement. It will also have the opportunity to bring about substantial improvements in the quality of its faculty. And it may be able to improve its drawing power for students. Much depends on whether it can increase its growth of voluntary funding faster than the growth of public sector funding. Substantial additions of federal funds appear to be unlikely. To sum up, the chance of finding some windfall solution to our problems is slight, and we will be increasingly constrained throughout the 1980s.

To conclude, we could be described as entering a new era of limits, something unimaginable in the optimistic atmosphere of the early 1960s, only dimly perceived as possible in the early 1970s, and now upon us in the early 1980s. All of you will more than earn your salaries during these coming years and as a result you will probably relish early retirement, particularly if the incentives are favorable enough. I wish you well in your work and in your efforts to devise effective ways of coping with limited resources, the aging of our faculties, and the special difficulties created by the change in mandatory retirement.

Comments

J. Russell Southworth

Mr. Southworth is a principal of Tillinghast, Nelson and Warren, which is a national firm of consulting actuaries. He is the manager of the New England Office and has more than twelve years of service in employee benefit consulting.

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It is really nice to be in a position to make sure that there are questions being asked. One particular comment I have is that if in fact we move to age 70 as a mandatory retirement and you have to provide benefit credit to that time, there is no question in my mind that most of your schools are going to have to readdress your entire defined objective and the accumulation that you'll have to provide is something less because the longevity is less. This, in fact, on the optimistic side, will end up enabling you to actually reduce fairly significantly the contributions on your existing program, maybe to the extent of 25-30%, depending upon how you might use your projections.

Now, the problem with this of course is, and again, I'm talking here to try and stimulate some discussion, the problem with this of course is that a lot of people are unable to work until age 70 or do not want to, so that you'll probably find yourself having to come up with some sort of early retirement inducement, whether out of necessity or to allow these people to get out in terms of the deadwood problem.

Now, the dollars that you will save immediately by reducing contributions to meet a benefit target at age 70 will enable you, if you work, to earmark a certain amount of this savings, and certainly not all of it is required, to come up

probably with some very generous early retirement schemes to enable people going out prior to 70 to have as high an income as they otherwise would have had if they worked until 70. So I don't think it's all on the bad side.

I think you will have to come to grips with that particular problem of reducing the contribution levels for existing faculty. The reason you will end up obviously saving some funds is that all good schools end up having people leaving your institutions along the way, and you're not going to have to provide those early retirement schemes - it's going to be the next employer. And to the extent that these people actually leave educational institutions entirely, it becomes a savings collectively to all of you.

Another thing we seem to be running into to some degree in some of our schools - we've asked repeatedly, because of inflation, because in certain cases you have defined contribution programs that might be integrated with Social Security, that is you provide a higher level of contributions on salaries in excess of Social Security. There's been a concern that as the Social Security wage base goes up much faster than inflation, that obviously the faculty are losing in the aggregate in terms of contributions going into their plans, and what's this doing in terms of not meeting retirement income objectives that we established previously?

Well, amazingly enough, in spite of the inflation and the rapid salary increases, although not so rapid according to Lee, for faculty, and the fact that on integrated plans contributions as a percentage of pay are actually getting smaller, the benefits at retirement are actually becoming larger as a percentage of pay for one simple reason, that; when you take you accumulation at retirement and convert it into an annuity, you're converting it on an interest rate that has been going up consistently at TIAA from 1970 through 1980.

The problem is this. I know that TIAA, for instance, is now moving its interest rates from 9 1/2 to 10 1/2%, thereby providing even that much greater annuity on a given accumulation. The only way that we can sustain, or TIAA can sustain, a 10 1/2 - 11 1/2 interest rate on its existing portfolio obviously is for continued inflation. In fact, the only reason that longer term fixed income obligations yield 11 and 12 and 13% is because of a perceived inflation rate of something like 10%. So suddenly to focus on what has been the traditional way of looking on benefits at retirement to see if they are meeting adequate income objectives, when you take that into account with Social Security, I think maybe is the wrong way to look at it now, particularly when you snapshot at that one age and then find a tremendous erosion over time, particularly at 8 or 9 or 10%.

I don't have to tell you how much erosion you do see. And particularly with faculty members where Social Security which is fully indexed provides 25% or less of a person's total income, the total erosion factor is fairly large.

These are comments, frankly, just to try to stimulate some discussion. I do have a question of Laura. I think she mentioned at one point that the longer the EEOC proposal does not come out, the better chance it has, in terms continued pension credit, of not becoming law in the future. Do you actually feel that that might be the case? I think a lot of people are assuming that both defined benefit and defined contribution plans will have to provide credit right up to the new mandatory retirement age.

Questions and Answers

Q: What do you foresee happening with the apparently differing interpretation of regulations by the EEOC and Department of Labor?

LF: The Age Discrimination and Employment Act actually technically is an amendment of the Portal-to-Portal Pay Act, with which many of you labor lawyers and economists are probably familiar, and that law contains a provision which exempts employers from any liability that they may incur through good faith reliance on regulatory interpretations by any administrative agency. So I think schools, for however long the Department of Labor's interpretations stay in effect, will be protected from any liability for anything that happens during that time. As for the question of whether the EEOC is likely in the future to change Labor's interpretation - I do get the impression that, as I said, they are gun-shy as a result of what happened to them in the Gilbert case. If all of you are not familiar with General Electric v. Gilbert, that was the pregnancy disability case in which the Supreme Court of the United States said almost in these words that the regulations of the EEOC are not worth the paper they are written on, in a situation where they had flip-flopped and just had behaved very badly. As I indicated, based upon the wording of the statute, I think that a case could be made that the contributions should continue, and it's not inconceivable that the EEOC people will come out with regulations to this effect. But 16 months have passed; they've gotten all the comments from the other agencies, and they are just sitting on it, and I do think there is some gun-shyness there. Maybe they are waiting for the election, who knows? I certainly couldn't give a definite indication one way or the other, but I do think that the more time that passes, the less likely it is because the movement will have lost whatever impetus it had. I think the aging

advocates have forgotten about it.

Q: Your comment about early retirement leads me to mention ~~the situation at Wesleyan. We've~~ had a few of our outstanding professors leave, and ~~found it gave early retirement respectability.~~ Isn't this what we should be trying to do?

LH: Perhaps I did not address this issue in the context of my concerns about the erosion of faculty salaries. Let me try to link these two points. A year or so ago I attended a conference on faculty salaries and outside incomes; that conference was background for a Carnegie-sponsored report that will be out soon, calling for greater regulation of the outside activities of faculty members. One interesting concern expressed by faculty from the California system, where faculty salaries have lagged very seriously, is that some of their best colleagues are the ones who are leaving. They are going off to private industry, banks, corporations, and so on. The lag in faculty salaries is causing the best people to leave, and everybody is suffering as a result. Faculty members with good alternatives in the private sector are taking advantage of them, given the change in relative earnings situations in those two sectors plus the fact that you can earn more outside academe. To the extent that you have this happening already and now in addition you dangle these early retirement inducements in front of people, you may give them a double barrel reason for leaving. Certainly, you may give respectability to the program, but you could end up helping to nudge some very good people to leave your institution. This is not going to happen frequently in the humanities, but it will certainly occur in the sciences, engineering, the professional areas. As a result you may develop imbalances in the quality of your faculty that could be very serious. As I look at the 1980's, I see this as a major reason for concern — the

decline in the real values of the faculty salaries and the decline vis-a-vis what people can earn in alternative employments. This will not occur for everyone but perhaps for half or a third of the faculty who are in fields where they can transfer their skills and sell them in the private sector. Thus, attractive early retirement programs may be accentuating another problem and a serious one.

Q: Early retirement plans are a good thing if the person actually retires, but not so good if he goes on to another job. Could the early retirement subsidy be stopped if the person is employed?

LH: I know double dipping is pervasive and I'm not sure that there's anything that can be done to prevent it.

Q: But don't you think this is a waste of money?

RS: It's wasteful from one perspective; it's not from others. So, I think that might depend a little bit upon when your early retirement program is going to be coming into effect. We're talking about something that might be coming in any time after age 55. I think you've got to integrate, in some fashion, post retirement funds, so to speak, with special subsidies, but this also I think bears more on a point that I made a little bit earlier here: if you have your existing program as is, which presumably, at least at retirement, meets your retirement income goals at age 65, and then are forced to continue to make contributions beyond 65 or 70, then very clearly you'll be exceeding at retirement at least the goal that you initially have established. In fact, to a large degree, even if you don't make contributions beyond normal retirement, because of the interest and mortality factors, you will be exceeding the goals that you had set at normal retirement. Now, when you are confronted with

this faculty member who may not want to leave, and you are now trying to provide some form of financial incentive for him to leave, then you're going to have to meet not just the retirement income goals you initially established, but something much greater. After this is done a while, and you see the kind of expense you are looking at, I think most institutions are going to find that they have to cut the contribution rates that they presently have if, in fact, they are meeting existing targets.

Q: If the contribution rates are reduced, should this money be returned to the faculty member now, or used to insure adequate benefits after retirement?

RS: I'm probably going to be treading on a few other people's territory in later talks, but I think coming back again to this basic focus and the fact that we're looking at retirement income and seeing this terrific erosion after retirement, something is going to have to be done. In one sense, if the institution is merely meeting its retirement and annuity rates based upon today's value of money, and they really mean what they say in terms of wanting to meet certain objectives, then they are going to have to back around and provide some form of post retirement indexing, whether it be on a pay-as-you-go basis or prefunded, which can become terribly expensive if they wait too long. They are presently spending money that they could otherwise use for that very purpose. Conversely, there is another way of doing it, and it would be to look at the fact that maybe our real rate of interest has never been much more than 3%, and that might even be optimistic to some degree, and to look then at the income that could be produced by buying annuities from TIAA at 3% and letting this excess interest be used to take care, at least in part, of the inflation problem in the future. What you'll

probably find in most of your institutions right now, though, if we look at this again and do projections to see if your contribution rates are meeting retirement income objectives on the assumption that that accumulation would turn into an annuity at 3% interest, they'd probably be falling quite short.

A: (from John Biggs and Tom Edwards) We'll talk about this tomorrow.

Q: You did not address, perhaps deliberately, the question of alternatives to tenure.

LF: No, it was not deliberate. I hadn't really considered that as a possibility. Having just read a draft of a paper that someone did on tenure, I was impressed with how firmly it is entrenched in higher education. Clearly, however, there are alternatives that perhaps should be explored more fully.

Q: When Boston University President John Silber suggested developing alternatives to tenure he got shot down. Tenure is a well established apprentice and review system. I have questions about how to make early retirement plans fair and targeted, perhaps linked to the median salary, and how to develop phased retirement plans to meet individual needs.

LH: As I understand the age discrimination amendments, it is ok to mandatorily retire someone, but not to offer them partial retirement.

LF: I think that what you're saying is an accurate description of the state of affairs while the exemption is in effect, the reason being the ADEA prohibits discrimination of any kind in any terms and conditions of employment with a narrow exemption card dealt that says to colleges and universities: you may require retirement; you may

continue to require retirement at age 65, but by implication you may not do anything else that would be discriminatory on the basis of age. It's a strange result — I admit. It's as if saying, well, you can have capital punishment and execute these people, but you can't inflict ay lesser penalty upon them. (That's reasoning by analogy; I don't mean to say that retirement is execution).

Q: What about offering partial retirement?

LF: You may offer it; you can not require it.

Q: Can you retire someone, then rehire him part-time?

LF: Well, I think that you would have a problem convincing a court that you did in fact retire him... What is the difference between retiring someone and hiring them back on a different basis and shifting their terms and conditions of employment? Well you can say, maybe we'll have one day or one week or one month in between the two in which this person is not affiliated with the college. Then you say, well how long does that have to be to make it clear there really is a severance and that you really have divorced yourself from this person and then brought him or her back rather than just changing the terms and conditions of employment, which you can't do on the basis of age? Many people thought when this law was first enacted of various configurations just as you describe, and I don't think anyone has had the courage to try it; it's just too risky legally.

Q: Given all the problems with determining the amount and period of contributions to our retirement plans, how long can we go on with defined benefit plans?

RS: Well, you said defined benefit plans. By

and large, most faculty are covered, private faculty anyway, are covered under defined contribution plans. Right now there's a President's Commission, as you may know, on retirement policy, and they're looking at the problems you are having with income security via vesting. Outside of the academic world, in the corporate world, you typically have ten years required to be vested in a pension, which is typically a defined benefit plan. Now, they are talking about reducing the time period required to become vested so that if a person moves around, when they finally retire, they've got their full pension. But what they are, of course, finding, which they didn't realize before, is that because of the way defined benefit plans work, if individuals move around three or four times in their career, with 8 or 9% inflation rates, pensions from those earlier periods are based upon salaries that were so much lower than what they are earning when they finally retire that it doesn't really matter if they are vested or not because they are vested in practically nothing. People are realizing, maybe for the first time -- I know TIAA will like this because they've been advertising it all along -- that defined contribution plans are the answer; that if you are now sitting down to try to address this problem for the first time with a white sheet of paper and saying you want to be sure to allow mobility in the work force, you probably would take X% of compensation and say one piece of that is going to go into some form of deferred income which he can tap when he ultimately retires but can't get at sooner. And the problem is we're not working with a white sheet of paper, and to now go back and start from scratch, if we go to a defined contribution plan for the future for everyone, will take years and years to come out the way we want because so many people are close to retirement. I think clearly you are going to see continuation of defined contribution plans and

probably start seeing more of them in the corporate world. But at the same time, I think that if we are going to move to age 70 in some form, and more and more people are going to work till age 70, you are going to see some form of defined benefit supplement, however you might couch it. I don't see a way around it, frankly. And right now, a lot of corporations - they're fairly fortuante right now - can freeze benefits at age 65 for the rank and file although they can work till 70. They are also fortunate because these people don't seem to like their jobs as much as faculty members, so it's a little easier to get them out. What they're doing in a lot of cases is counseling the typical employee who might earn $25,000 or $30,000, the salary of a faculty member, and saying, ok, you can work until 70, but understand the implications of your working. Number one: you're foregoing Social Security, which, although you'll get a little bit larger benefit if you defer, it's not nearly as much as its actuarial equivalent, so you're looking at essentially one-third of your income from Social Security. You're not getting your pension at all, which is going to be frozen, so presumably the institution's able to take that money and feed it into salary. You can turn around then and tell the individual that I hope you like your work because you're essentially working for one-third pay. Now, what's happening there is it's getting these people to retire, and because of the earnings test under Social Security which is going up to $6,000 very soon, they are able to bring these people back on a part-time basis, maybe utilizing them very well. Although as an actuary I can't get into the other issues of how important it is for people to work after retirement, they are using them one or two days a week, taking full value of the Social Security setup the way it is right now, and at the same time allowing them to tap into their pensions. If you have some form of defined benefit superimposed over your existing defined contribution plan, you

can accomplish the same thing on a part-time teaching basis, although I don't know what might happen if they then can go to full time after they've been working one year at part time. I do see that this could be something that probably could be utilized within colleges and universities as well as corporations.

Q: There's the possibility of raising the age for Social Security benefits to 67, 68 or 70.

RS: You mean age at entry or normal retirement age of Social Security?

Q: Normal retirement age.

RS: Yes, but their problem is long term funding — that's getting into an entirely different issue. It does look like one of the prospects will be some form of postponed retirement, but maybe not to take effect until some distance into the future, in the year 2000 or so. For the next ten or so years you'll continue to maintain normal retirement to 65.

Q: This whole situation may be helped somewhat as there will be fewer new Ph.D.s coming along due to demographic factors. Also, institutions may stop hiring people at the full professor level or try things like job sharing or awarding research tenure vs. teaching tenure.

Q: If you hire a husband and wife with one salary, one set of benefits, what do they do with their free time?

A: (from audience) Work-research-babysit.

LH: Changes in the supply of new Ph.D's are interesting. Allan Cartter's projections in his 1976 book and several earlier papers indicated that Ph.D. production would continue rising --

forever! If you examine the National Research Council's annual summary report on Ph.D.'s granted, you'll see the number of Ph.D.'s increasing dramatically for a number of years, hitting a peak in 1974. Since then Ph.D. production has remained constant or fallen slightly. This reflects a tremendous response to market conditions and perhaps to other forces as well. Of course the number of Ph.D.'s granted cannot drop to zero, because Ph.D. students are an essential input to teaching and research, especially at big universities. If the number of economics graduate students went to zero at Wisconsin, we'd be in peril; I don't know what we'd do. This is not a problem at four year colleges, but it certainly is at universities. There are also differential responses in the different fields. Physics has had a very rapid drop off; education may still be rising slightly. So you find very different patterns across disciplines reflecting, in part, changing market conditions and, in part, other forces that I'm not really sure we understand. I don't believe that you will ever get a big enough response to choke off supply so the market will generate salary increases of the kind we might observe in other occupations. If that did happen, we might be in an even worse situation. Let me take up your other point about hiring full professors. Harvard replaces a full professor who dies or retires with another star from somewhere else, and that institution in turn hires someone from another institution, and that process continues on down the line, and eventually another assistant professor is hired somewhere. While an institution may change its faculty age and rank structure somewhat by virtue of hiring a senior person rather than a new Ph.D., for the academic sector as a whole nothing much will happen.

Q: The question is, still remains, what do we now want, and what should we be doing for the future?

LH: Well, it's not a question necessarily of what we want. As I recall you had individuals coming in and testifying before Congress, and I'm sure that people like Bill Bowen and John Kemeny offered advice. As I understand it, Congressmen didn't know anything about this matter; they simply didn't know what to do. They were eventually persuaded that they should not act too hastily. They decided to have the question studied and to delay final action. Now they will want to see what comes out and then decide. That's one issue. The other one is this: Irrespective of what the studies show, what should we be doing to help achieve what we want whether based on the study findings or the other ideas of faculties and institutions? Already things have changed because many states have raised their retirement age to 70. I am now trying to digest all the state and legislative changes, most of which have followed the federal legislation. So if you want to go back to the pre-1978 situation, then you've got fifty states to work. This will be difficult if not impossible to handle. All you can hope for is that a persuasive case can be made at the federal level that may lead the states to behave in the same way. It is important now to think ahead and try to figure out what you want rather than waiting, as happened in 1977-78, until the horse was out of the barn and then trying to move quickly to affect the legislation.

Q: In terms of ERISA, what can be done to get rid of someone who won't retire?

LF: I think it would be gross incompetence on my part to answer any questions about ERISA. It is a many-headed monster that only people who spend their lives on it could credibly comment on.

Q: Well, can you make payoffs of a couple of years' salary if that's what it takes?

LF: Well, a tenure contract is a contract like any other, and the terms of it can always be revised by mutual agreement. That's true of any contract, so if the other parties were willing, then you'd rewrite it to your specifications -- whatever dollar amount you wanted to [illegible] on it. The danger would be that he or she [illegible]t claim later than there was coercion involved but that can always be the case.

Q: What are the tax consequences of contributing such a lump sum to TIAA/CREF?

RS: Well, clearly there are exclusion allowance limits to how much you can put into TIAA or CREF. There are ways in which after a person actually disappears from the institution and no longer has a salary, that you can continue to put funds in TIAA and CREF but typically it would not be up to one or two times pay, so probably the way you'd do that would be to give them some sort of compensation and enable their TIAA/CREF benefits to grow to that level that you'd otherwise want to get. So you get there in a different way but you get there in a much more tax efficient basis. So in other words, instead of just dumping a lot of money into TIAA and CREF, running amok with the exclusion allowance and creating tax problems for the individual to allow them to live on a reasonable retirement income, you determine how long it will take for that TIAA/CREF to accumulate to the level that you want to pay him and then in the interim you pay him some sort of bridge.

Q: I have one question that really comes to Dr. Hansen and to anyone else who might know: I am really worried about the fact that none of us has been looking very hard ahead at the problem of possibly having total uncapping. I'm wondering if anyone knows if there's anyone responsible for doing a study or thinking about doing a study about the subject?

With the total uncapping, we would then be faced with a situation as now exists in some states with the no-mandatory retirement age allowed. We would then have people with contracts without an end date, known as tenure, and no possibility of having a mandatory retirement age at all.

LH: The difficulty with trying to answer the question is that there are almost no institutions that do not have some ultimate mandatory retirement age. This makes it difficult to check the experience of schools with no cap. For this reason, there is no way to project what might happen at institutions after they are uncapped. This is something that we will try to address in our report, but I don't believe we can do it very effectively. Perhaps we can only write a couple of sentences on the matter. Yet this is a very important question that we should be trying to figure out how to analyze. If the cap is taken off, all of you are going to have to work a lot harder, I'm afraid, in doing whatever you're trying to do to encourage early retirement or to deal with people who plan to continue but who should be retiring.

Q: It might be of some use to look at the experience of the federal government, where there has been no mandatory retirement age for several years.

RS: Historically, we got the mandatory retirement age in the 1920's because the federal agencies felt that if they didn't put one on they couldn't ever get anybody out.

LH: Yes, but the extent to which you can generalize from the federal experience is unclear. And its experience is not long enough. Yet we are going to have to consider it as best we can.

A: (from audience) Well, the uncapping comparison can only be carried so far, because the federal pension system is indexed.

LH: Except that most public institutions have defined benefit programs which are the highest three years multiplied by the years of service times X, and so in that sense we might have counterparts to the federal system, but without the indexing.

SECOND SESSION

Presiding:

Katharine H. Hanson
Executive Director, COFHE

"Retirement and Inflation; The Problem, Qualifications, and Some Modest Proposals for Change"

Speaker:

John H. Biggs
Vice Chancellor for Financial Affairs
Washington University

"The TIAA/CREF Perspective"

Speakers:

Thomas Edwards
Chairman of the Board

Donald Willard
Executive Vice President

John McCormack
Vice President

Commentator:

Robert F. Link, FSA, MAA
Consultant

"Faculty: Planning for Retirement"

Speakers:

Janice Clinthorne
Project Director, Retirement Plans and Related Factors Among Faculty at COFHE Institutions
Institute for Research on Social Behavior

George Barbee
Executive Director
Consumer Financial Institute

Moderator:

Aaron Lemonick
Dean of the Faculty
Princeton University

Retirement and Inflation

The Problem, Qualifications, and Some Modest Proposals for Change

John H. Biggs

Mr. Biggs, a graduate of Harvard, is now a Vice Chancellor at Washington University. Prior to his university career, he served for many years as an actuary and then as a senior manager with the General American Life Insurance Company of St. Louis.

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Thank you. I suppose all of you have noticed by now that we're having this meeting at the corner of Benefit and Benevolent Streets, which is a great place for this kind of meeting. You're also getting a heavy dosage of actuaries at this meeting, porbably heavier than you have ever had in your previous career or ever will want to have again. Bob Link, who will be commenting on this session, is an actuary. I am an actuary, and Russ Southworth, who spoke yesterday, is another. One of the things actuaries like to do is tell jokes about actuaries and we don't get a chance to do it often because most actuarial audiences have heard all of them. Hence this is an opportunity that we can't miss. I have two short ones, which will help define for you what we are. The first definition is simply that an actuary is a person who wanted to become an accountant but didn't have the personality for it. The second was found in a very scientific way. Somebody decided to do a study of what people thought actuaries were, so they put people out on street corners asking passers-by what they thought an actuary was. And one solemn citizen said, "Well, it must be a place where you bury dead actors." Having imposed on

you with those helpful definitions, let me move to our cheerful subject of inflation and retirement.

Most Americans today believe there is a high probability of double-digit inflation for the almost indefinite future. This is reflected most clearly in the financial markets where long-term bonds no longer can be sold without a roughly 10% "inflation premium". In the past, most American financial people have been unwilling to use such a doomsday prospect in doing financial planning for themselves or for their institutions. The evidence accumulates, however, that a double digit inflation rate is with us and that we need to at least think through the implications of such an experience. Accordingly, I plan to present the implications of an indefinitely continuing 10% inflation rate--that is the problem, then some mitigating circumstances, and finally several proposals to defend against the effects of such an inflation. What would a 10% permanent rate of inflation mean to a faculty member in his mid-sixties contemplating the possibility of retirement? What actions can be taken by those of us responsible for the retirement systems of higher education? These two questions are another way of writing the abstract for this paper.

The Problem

For the purpose of illustration, let us consider a 65 year-old professor earning $35,000 a year with a current TIAA-CREF accumulation of $100,000. From my review of the COFHE materials and the detail of our own faculty situation, this is a fairly typical result in 1980 for a career Arts and Sciences professor. We will also assume his university had the good sense to stay in the Social Security system and he did not opt out personally. As the subsequent analysis will show, the difficulty of the questions we have asked focuses on approximately this salary level -- with

somewhat easier solutions for lower or higher salaried individuals.

Under present TIAA-CREF procedures, this professor (assumed male but soon to be unisexed) could begin drawing in 1980 an income of $12,300 from TIAA or $8,200 from CREF. Intermediate figures can easily be interpolated for various fractional allocations between TIAA and CREF. I have assumed a "straight life annuity" — i.e., there is no continuation to a spouse or beneficiary after death. In actual fact, many faculty elect a joint annuity, providing benefits for as long as either the faculty member or spouse survives — which makes the period of concern after retirement significantly longer. Also, I want to come back to the difference in the initial payments between TIAA and CREF.

Now for the bleak picture. At 10% inflation, this income steadily and rapidly declines in real value as follows:

Year	Age of Pro-fessor	Purchasing Power Rela-tive to 1980	Income in 1980 Dollars	% of Retirees Surviving
1980	65	100%	$12,300	100%
1985	70	62	7,600	91
1990	75	39	4,700	79
1995	80	24	2,900	63
2000	85	15	1,800	43
2005	90	9	1,100	24
2010	95	6	700	8

Accordingly, if our professor opts for a fixed income under TIAA, his real income will be seriously reduced in just five years, cut to 39% in ten years, and virtually eliminated in twenty. Since a significant percentage live to age 85, it seems that our entire private pension system is seriously flawed. Our sacrifices in income prior to retirement in order to provide a future

retirement income end up producing a sort of declining transition income from retirement until ten to fifteen years later when all the retiree has is Social Security income.

The problem is not one for just a few unusual people who happen to live to a ripe old age. Using the mortality table underlying current TIAA-CREF retirement conversions, the following percentages survive to the ages shown:

Age	Percent Males Surviving	Percent Females Surviving	Percent Where Either or Both Survive
65	100%	100%	100%
70	91	95	99
75	79	89	98
80	63	78	92
85	43	61	78
90	24	39	53
95	8	17	24

Since most TIAA annuities are joint annuities involving a faculty member and spouse, the third column is the most important one. In only 8% of the families have both died before age 80 when, under 10% inflation, the TIAA benefit has been knocked down by over 75% in real purchasing power. Note the surprising result that one in four families will still be relying on TIAA-CREF income at age 95.— thirty years after retirement.

Thinking about this simple illustration may give all of us pause; fundamental questions are raised: why try to save anything at all? and if other Americans think the same way, where will needed capital for business and housing come from? This line of reasoning supports the following insidious syllogism: (1) government will continue to cause inflation; (2) Social Security is indexed but private employers cannot afford indexing; (3) the government must prevent even implicit "fraud"

and over-promising by employers; (4) accordingly, private pensions must be outlawed; and (5) all pensions must be provided by Social Security. This argument has been forcefully presented by several economists to the current President's Commission on Pensions. But we should not wander from the practical things we and our institutions can do.

Qualifications

What lightens this doomsday picture?

1. Indexed Social Security Benefits.

The most important mitigating fact is that our professor will also be entitled to annual Social Security benefits of $7,800 in 1980 (plus an additional $3,900 if his wife is 65 years old). Under the current statute, these benefits are indexed and under continuing 10% inflation, would rise by 10% a year. Consequently, our professor's revised nominal and real incomes would be:

Year	TIAA	Social Security	Income in Total Dollars	1980 Dollars or Real Income	Percent of Initial Amount
1980	$12,300	$ 7,800	$20,100	$20,100	100%
1985	12,300	12,600	24,900	15,500	77%
1990	12,300	20,200	32,500	12,500	62%
1995	12,300	32,600	44,900	10,700	53%
2000	12,300	52,500	64,800	9,700	48%
2005	12,300	84,500	96,800	8,900	44%
2010	12,300	136,100	148,400	8,500	42%

We should also remember that under current law, Social Security benefits are not taxed so that the after-tax real income of our professor will be reduced somewhat less than the table shows.

Also, if the professor has a spouse, there are additional Social Security benefits while she lives.

2. CREF

One of the most significant financial innovations — in the insurance, banking, or investment industries — in the last thirty years was the variable annuity, and TIAA-CREF can be proud to have been the pioneer in the early 1950's development. Private life insurers did not begin offering such annuities until the late 1960's. I was personally involved in the product design for one company at that time, and, like all other actuaries, my first step was to read the classic 1954 paper by Robert Duncan, who at that time was the TIAA actuary, and who worked through the theory of equity based annuities and the practical institutional application of that theory.

Yet, we all know the disillusionment of the last decade with common stocks as a hedge against inflation. But our projection here is for a professor not over just ten years, but over twenty and thirty. Even with the declines of the 1970's, stocks have produced better real returns over twenty and thirty years and do have a good chance of substantially off-setting inflation. If stocks did give a real return of 4% over the professor's lifetime or approximately 14% nominal return if inflation is 10% — and there are some good reasons to believe they will — then the CREF income would rise 10% a year and our professor would come out even against inflation (except for income taxes). In fact, a 90-year old today who retired in 1955 at age 65, would have done extraordinarily well under CREF in spite of past inflation.

I should explain briefly my exception on federal income taxes. My projections in this paper abstract from any possible changes in the

income tax structure — including possible future taxation of Social Security and possible indexing of tax brackets. I'll point out at each time the rough implications of taxes but projection of what Congress might do is even more chancy than projecting inflation rates.

In any event, a retiree today with half his income from CREF and half from TIAA need not look at Table I's bleak "certainty". He has a realistic probability of preserving much of his income. Unfortunately the word "probability" must be used and retirees are in the weakest position to take chance.

3. Other Assets

It seems fair to assume that most 65 year-old professors will own their own homes and will be close to the end of their mortgage schedules. Accordingly, for a major item in his budget he is relatively protected from inflation -- at least as to the capital costs of the house. Utilities and maintenance will run up with inflation. If at a later age an apartment is preferred or, in the case of bad health, a nursing home, the appreciation due to inflation of the house will provide a significant capital source.

For those with higher incomes than our example, there may well be still other assets -- a summer home, an investment portfolio, and probably some life insurance cash values. Those with lower incomes will have a larger proportion of their income provided by Social Security.

Of course there are counter examples -- there are 65 year-old faculty who are still confronted with costs of aging parents and some with college tuition bills for their children.

4. Medicare

Another major item in the family's budget is virtually inflation-proof to those over 65 — health care. At current prices it would cost more than $2,000 a year for an individual to buy the health benefits provided by Medicare. And, of course, as prices rise, the Social Security system automatically improves the value of these benefits — except for the small supplementary premium and the hospital deductible.

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5. CPI Overstatement

Our barometer for inflation has recently come under a lot of deserved criticism. Clearly it is not a good measure for cost of retired professors' living standards. Although it may not include enough for books, wine, and travel, it includes way too much for housing, probably for automobiles and gasoline. After retirement, commuting costs are reduced and, hopefully, there is less need for station wagons to provide children with taxi service. Quality changes are badly handled in the CPI and the measured market basket does not include the benefit of government regulation.

The overstatement should not be "overstated," but it is probably worth 2% to 3% out of the recent 1970's rates of increase.

Given the above qualifications, the situation facing retirees is not quite so bleak, and there are strategies and options (particularly CREF) that may help a good deal. We are still left with a nagging uneasiness that universities as employers have further obligations. And I'm sure TIAA officers are acutely uncomfortable when they consider the implications of this scenario for TIAA.

What Can or Should We Do?

First off, a point about financing Social

Security costs should be made. The rapidly rising income benefits and Medicare costs for retirees from universities will be paid for by someone and that someone turns out to be universities themselves. Next year we have a healthy 24% tax increase for anyone earning over 30,000. In large part that will be used to pay for the 14% increase in benefits to retirees that was awarded this last July 1st. Similar increases will be imposed in the future -- hopefully not at the 24% level -- and, of course, universities as employers will have to pay half the cost and employees the other half. In short, when our professor retires our government has already mandated that we will pay for his indexed Social Security benefits.

Can TIAA type pensions be indexed or defined benefit private pensions be indexed? The critics of private fixed annuities say they cannot and therefore seek government solutions. Let us not too hastily reject this idea of indexing -- in fact, the key proposal I want to make in a few minutes is that there is a form of "capital markets indexing" or "modified indexing" that is clearly feasible.

Let me set out the argument that, at first blush, seems to condemn the idea of indexing private fixed annuities. Another way of looking at our example of the typical [illegible]HE Arts and Sciences professor is that we want to provide an initial income at age 65 of $12,300 and the cost to do so is $100,000. What additional cost would it take to buy him an increasing income that starts at $12,300 and goes up 10% a year thereafter. Using the present TIAA prices -- reflected in their mortality, interest and expense assumptions -- the extra cost is $134,000 for a total of $234,000. One can quickly trace out the implications for universities in such an addition to costs. In fact, the result is really not a way to index real income because of the terrific increase

in federal income taxes that would eventually evolve.

But we shouldn't stop here. The price for $12,300 in retirement income has dropped dramatically in the last two decades. Interest rates used by insurance companies to calculate single premium annuities have gone from 5% in 1960 to 12% or 13% today. Although people live longer, this change in interest rates dwarfs that effect. Surely in defined benefit pensions some of that savings might be used to provide a form of indexing -- perhaps not CPI indexing but at least providing for current retirees the same real costs that were spent on past retirees. This is complex and not precisely relevant to TIAA, since TIAA is a money purchase plan. I come shortly to my proposal for how it might be indexed.

Insurance companies, employers, and economists are all giving much more thought to indexing pension benefits. The proposals I've seen all involve fairly radical new financial instruments and hence seem to me remote from practical applications. For instance, if the government provided indexed bonds -- offering a return of, say 3%, that grew each year with the CPI -- such a bond might secure an indexed annuity commitment. However enormously difficult implications flow from such an approach. Another approach, outlined recently in a paper by an economist associated with the NBER, would offer an indexed annuity secured by short term investments hedged with holdings in commodity futures. The flow rate of return would only be 0% -- which makes for a pretty low annuity if inflation does abate. Again, the institutional arrangements are pretty difficult. These examples are to suggest only that imaginative financial innovations may be coming.

Another idea sometimes mentioned is providing insurance against "living too long". I interpret

this to mean that if our professor lives to say, age 80, there might then begin an income to compensate for his inflation losses. Apart from the obvious problems of discontinuity in such an arrangement, the costs are not inconsiderable, although a lot less than full indexing. A 10% per year rise in income for fifteen years causes roughly a quadrupling of income. If we allow for mortality probabilities and for a yield on investments of 10%, we would need $31,500 at age 65 as a single payment to provide a deferred annuity for our professor of three times his beginning annual income. Nothing would be paid if he died before age 80.

It would be difficult as a practical matter for a private insurance company to offer such a contract without some death benefit payable between 65 and 80. Results for other periods are not too different:

Projection Years	Increase Required if 10% Inflation	Cost at Age 65
10	159%	$38,000
15	318%	31,500
20	573%	19,700

Again, I bring up the progressive federal income tax structure as a caveat.

Some Ideas to Explore

The first idea that seems to me important is to help faculty cope with real and imagined fears of inflation in making their decision as to actual date of retirement. It will be unfortunate for the quality of our faculties, and the quality of life for the senior faculty members themselves, if our retirement arrangements induce faculty to stay on longer than they want. Surely, the faculty member eager to retire -- for whatever reason --

but induced to stay on, even to as late as age 70, by his or her fear of inflation, is not likely to be a great teacher nor a productive researcher in those reluctant continuing years. What we must do is neutralize the retirement decision so that the inflation fear does not dominate.

This was perhaps the primary objective behind the design of the Washington University "bridge benefit". Since it is fully described in the COFHE materials, I will not go into its detail here. Fundamentally our plan involves a defined benefit at age 65 with inflation protection until the mandatory age 70.

A second reform I would like to see made is in the TIAA annuity program and this is perhaps the central idea of this paper. It seems to me that the rising interest rates of the 1970's, along with increasing inflation, have altered significantly the desirable design for the TIAA "fixed annuity". This is a bit complicated, so please bear with me.

1. In determining the annual income from an annuity, an interest rate must be assumed -- called the Assumed Interest Rate or AIR. Currently TIAA earns 9% to 10% on its portfolio of investments and uses a rate of 9.5% to begin annuities (part of this is not guaranteed and could be reduced, which is unlikely if inflation continues at 10%, since interest rates will undoubtedly rise still higher). The AIR used for CREF is only 4%. I'll come back to this.

2. The annuity income can be thought of as two parts: part an interest or investment income return and part a return of original capital (the latter distinguishes the annuity from a simple investment), hence

the higher the interest rate, the higher the income. The return of capital reflects the mortality experience expected for the group of lives.

3. TIAA is basically a fixed annuity -- the income you start with will be fixed over your lifetime (the small exception is that if TIAA does much better than assumed on your money, you get the results through a dividend supplement). CREF, on the other hand, is a variable annuity; it is fully expected that CREF annual payments will vary substantially and will do so in accordance with the results of the underlying portfolio of CREF equity securities. The AIR for CREF is 4%. If the stocks do well and earn 20% in a year, the income goes up roughly 16%. If badly, say the return is -10%, then the income drops 14%.

Given that brief discussion, I come to my proposal. TIAA should also be a variable annuity assuming 4% as the AIR as does CREF. What would this mean? First off the initial income to the retiree would be lower and would be equal precisely to that for CREF. As the fixed asset portfolio of TIAA earns more than 4%, the income each year would rise. If, for instance, in 1980 the funds for our professor earned 10%, his income the next year would rise approximately 6%. If inflation does continue long at 10%, interest rates on taxable bonds will surely rise to 15% and probably higher. At 15%, our professor's income would rise by 11% a year (TIAA has, of course, a lag in its portfolio returns as interest rates change -- but over a ten to twenty year period, this would work out).

There is a clear economic theory underlying this plan. Nominal interest rates on bonds, say 13% today, are seen by economists in two parts:

one is a real interest rate of probably 3% or 4% at most, and the balance is an inflation premium. All of us responsible for college endowments know this and have changed our spending policies to plow back at least part of the inflation premium. The TIAA annuity design in the 1950's was simple and sensible. TIAA used about [illegible]2% and CREF's rate was 4%. Inflation and consequent higher interest rates have fouled up the relationship. Both then were annuities in real income; CREF remains so but TIAA is now mostly nominal and seriously misleading illusions follow from that — a form of irrationality that economists call "money illusion".

The idea of making TIAA a "variable" annuity based on 4% interest is not an impractical idea. The variable annuity principle for fixed asset portfolios was adopted by the life insurance company I worked for; they did so in 1969. We referred to it as a "monotonic annuity," since we guaranteed the AIR — the annual income could only go up. And we used a 3 1/2% as AIR. The whole rationale and technical detail are described fully in my paper published in the 1969 Transactions of the Society of Actuaries, which has been required reading for students taking the actuarial exams since that time. I'm sure some young actuaries at TIAA had to plow through the whole paper.

What would such an annuity option do for our professor retiring in 1980? I've set out below a plausible scenario based on continuing 10% inflation rates:

Age	(1) Projected TIAA Total Earnings	(2) Total Dollar Income	(3) TIAA Real Income	(4) Real Income as a Percentage of Initial Amount
65	10%	$8,200	$8,200	100%
66	11%	8,700	7,900	96%
67	12%	9,300	7,700	94%
68	13%	10,000	7,500	91%
69	14%	10,800	7,400	90%
70	15%	11,900	7,400	90%
75	15%	19,600	7,600	93%
80	15%	32,400	7,700	94%
85	15%	53,600	8,000	98%
90	15%	88,700	8,200	100%
95	15%	146,600	8,400	102%

Column 2 is derived by starting with a payout of $8,200 at age 65 using an AIR of 4%. (Note that $8,200 is the CREF initial amount.) The values in later years are found by multiplying the previous year value by a factor where the factor is 1 plus column (1) (in decimal form) divided by 1.04.

There are a number of advantages in the above results:

(1) Obviously the TIAA annuity income becomes responsive to inflation. The retiree doesn't "blow" the inflation premium each year but adds it back to his principal. And if inflation abates and interest rates fall, the annuity adjusts automatically to the new circumstances.

(2) There is no perverse incentive to get out of CREF into TIAA -- as there is now -- in order to get more immediate income per $1,000 of retirement fund. CREF and TIAA

then operate on exactly the same principles. This problem needs emphasis; the current policy of TIAA-CREF is to permit fairly easy transfer from CREF to TIAA. It doesn't work the opposite way. In fact the most dismaying set of data I've seen is the steadily declining use in the 1970's by our professors of CREF.

(3) The results dovetail nicely with the faculty member's mortality experience. Those who live to 95 will have a steadily rising income. Obviously, the plan is disadvantageous to those who die soon after retirement. If we want an insurance plan against living too long, this is it, funded simply out of the money already accumulated by the TIAA system.

(4) Another significant advantage is that if the faculty member starts out with $12,300, he pays tax on the whole amount and if he then saves some for later needs, he'll have to pay tax on the interest earnings from his investment. Under the proposed annuity, the portion plowed back is not taxed and its earnings escape tax until they show up as income much later. (The arguments for SRA annuities are precisely these arguments.)

(5) To avoid confusion, some name other than "variable annuity" is needed for this annuity. As I see its design, it should be "monotonic" or a "ratchet annuity" -- the income is only variable upwards. Without imposing a lecture on asset valuation practices of life insurance companies, let me simply say that TIAA uses book or cost values for its fixed assets and does not revalue them continuously to market, as does CREF.

Accordingly, in the current climate at least, it would seem that TIAA could guarantee the AIR of 4%. The mechanics of the annuity then assure that the annuity would only go up — as TIAA's average rate of earnings exceeds 4%.

(6) Another serious problem with the present TIAA annuity is the illusion of wealth created by sending out the blue and yellow projection forms each year. Current high fixed income earnings are used to project retirement incomes and our faculties look at projected incomes at times higher than present earnings. The result is reduced interest in additional savings and reduced pressure to allocate more of our salary and benefits budgets to TIAA and CREF. The fact is that they and we are all fooled by money illusions. Using 4% to calculate annuities and 4% to project them would give a realistic valuation of how well off our people will be after retirement.

(7) Other difficult plan design considerations exist. One is whether to give people options on the AIR. Our plan at General American did so but I think for TIAA that would not be advisable. A complicated form of mortality anti-selection would arise and the option would be confusing.

Let me rephrase my proposal in terms of capital preservation. At current inflation induced interest rates, our retirees eat into their capital both through the mortality principle but even more so due to spending the inflation premium. If TIAA used 4% interest, this problem would be substantially overcome.

And, finally, let me come to the obvious question. Could our professor retire on only $8,200 instead of $12,300? Counting Social Security, his initial income is reduced from $20,100 to $16,000 (exclusive of spouses' Social Security entitlement). The drop is substantial, but the benefits of significant inflation protection are also substantial. My preference, if I were the 65-year-old, is very strong for the $16,000 and rising income. However, and perhaps this is most important, if the reduction is too severe, then we, as university benefits planners and as TIAA annuity designers, have partially failed in our job. More money needs to go to TIAA so that the job gets done.

Q. What is the current rate used by TIAA for fixed annuities and what is it likely to be in the near future?

A. Presently it is 9 1/2%. I understand TIAA is likely to change to a higher rate in 1981 (The subsequent announcement is that the new rate is 11%). Those who retired prior to 1981 will have an increase in their annuities, reflecting their age, annuity option, and so on. The increase is not comparable, however, to the kinds of increase a "ratchet annuity" would experience.

Q. What will happen to TIAA's investment results if inflation continues at 10%?

A. TIAA pays to all annuitants the average rate earned on its total portfolio of investments. Today's 13% to 14% rates on new funds get averaged in with the lower rates on investments made in past years. Obviously if inflation continues and rates stay at 13% to 14%, or more likely rise to 15% to 16%, TIAA's average will

gradually rise. New funds will be invested at the higher rates and old lower rate investments will gradually mature and can be invested at the higher rates.

Q. Is there a case for TIAA to pioneer — as it did in variable annuities — with a retired person's price index?

A. I think the government already has such a project underway since the CPI has been under so much attack. Preparing an appropriate index is an enormous and costly project, involving national statistical sampling and difficult theoretical issues. The cost of designing an index must run to the several million dollars at least. I doubt whether one institution in the private sector should undertake such a project.

A further point is that all such indexes are at best very crude measures. Many theoretical economists have shown that such measures are seriously flawed at the theoretical level. The problem is then compounded by the practical computational difficulties. I just don't put a lot of priority on refining these measures. Inflation is certainly real and one of its worst manifestations is that it affects the welfare of different classes and individuals within those classes in very different and unmeasurable ways.

The TIAA/CREF Perspective
The Unisex Issue

Thomas C. Edwards

Mr. Edwards, a Phi Beta Kappa graduate of the University of North Carolina, has a distinguished career in the insurance industry. He has been associated with TIAA for thirty years, served as President for twelve years and is now the Chairman.

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I'm very pleased to be here. This is the first time I've ever been invited to a COFHE meeting, and I think it's terrific. I was saying to somebody at breakfast that when you walk around the halls at this meeting and hear everybody here talking about a subject that we eat, drink, and sleep 24 hours a day back home, it is really a rewarding experience to know that you indeed care and know so much about this subject. I hope we can remain a part of everything you do here. I think what's happening with the Age Discrimination in Employment Act and everything else these days, including double-digit inflation, has tremendous implications not only for higher education but for all of the private sector. Just one comment to John Biggs. We don't stop worrying about annuitants at 95 or 90. I sign a whole stack of congratulatory letters once a month to our 90-year-olds and the 95-year-olds. One of my predecessors a number of years ago said, "If we're going to lose, we ought to lose gracefully." And it's surprising and gratifying to see how many there are at those ages.

It's my job to introduce the TIAA-CREF people. That's John McCormack and that's Don Willard and that's it. John is going to talk about the ADEA implications for retirement plans,

a little bit more than you heard yesterday, and some of the flexibilities available within the TIAACREF system that help early retirement programs. You may not know about all of them. Don is going to talk about some of the pre-retirement planning developments. A very important part of any early retirement approach is to get people thinking about the fact that, "Hey, retirement actually comes, and it will affect me if make it to that age." I remember Allan Cartter at NYU once telling me that a professor, aged 68, showed up in his office with this little slip of paper, and said: "What is this retirement business? I didn't know I was going to have to retire." And that sort of thing is still with us, as many of you may know. Don is also going to talk about methods of coping with inflation, and just so that you will listen to me and John before we get to Don Willard, I ought to mention that we are already way past the conceptual acceptance stage of a program very much like the one John presented. We're into the systems and procedural work for an increasing annuity. I don't think we'll call it a "ratchet annuity" but that's still a possibility. We hadn't thought of that one. Don will tell you about the details of that and how it's done.

Now, I'm probably going to tell you a little more than you want to know about the unisex question and where we stand on that, because that's running through everything we do these days and has implications for you. We owe you an up-to-date report on it. You would have had a letter on it two weeks ago except for the position recently taken by the EEOC. This whole merged-gender situation is not a simple issue, as those of you who have gotten into it know. It's full of complexities and emotions, especially the latter. The blood pressure of both men and women gets raised about equally during any discussion of the subject, not only because it involves peoples' retirement savings; it also involves basic

questions of equity and fairness. And it involves a major change in the conventional use of risk classification and laws of probability, which have always been used in pricing insurances, pricing annuities, and in determining lifetime benefit amounts based on life expectancies.

I'm going to skip the background. It's been eight long years with nine court cases and continuing conflicts among federal regulators as to what's fair and what's equal in this business of providing lifetime incomes. Basically today the thrust of the regulators, the thrust of the courts, and now Congress is that in the future the civil rights of the individual as one person have got to prevail over insuring principles that classify people by age and sex into groups for risk sharing purposes. Age groupings are still okay; sex groupings are out, at least for insurance and annuities. At the federal level the actions being taken are all under Title VII of the Civil Rights Act and the Equal Pay Act. At the state level the actions are under the various human rights laws in the states. And the actions now being proposed in Congress by the Dingell Bill in the House and the Hatfield Bill in the Senate are all-inclusive. They're trying to fix it so that all insurers, all government pension plans, and everything involving lifetime payments, whether in an employment situation or not, will have to go to a unisex mortality table because anything else is "discriminatory." I learned this week that Canada is also moving strongly in that direction at the federal level.

Well, about a year ago, as you all know and as John Biggs has mentioned, our Boards moved toward meeting the growing concerns of a number of your institutions, a number of state universities, the ACE, and other education associations. We set out then to convince the various state insurance departments that in spite of their model uniform

laws, which require "equal premiums and equal dividends for individuals of the same class and equal expectation of life," it seems clear from the courts and everything else that the time has come to approve the use of a sex-neutral mortality table for future annuity premiums. Well, this effort has taken us a year, and where there were rejections among the various states, we went one-on-one with them. We explained how and why the legal and social tide is moving, and the states have all eventually approved the merged-gender table we proposed. We also announced a year ago that once we got these approvals we would adopt the merged-gender table for future annuity premiums, so that in the future equal premiums paid by similarly situated men and women would buy equal periodic benefits under all of the income options at retirement rather than just the joint-life options for a husband and wife, as at the present time. The annuities reserve the right to change the premium rates for the future, but we have no right or intention to change our representations as to any premiums paid in the past. Ninety days notice must be given to all participants for future premiums, and there will be no effect on TIAA benefits resulting from past TIAA premiums; no effect on CREF benefits resulting from past CREF premiums.

The prospective change will apply to both regular and SRA contracts, primarily because tax-deferred annuity plans and pensions are both considered employer "retirement plans" at the federal level, by the EEOC, the IRS and ERISA. There's also been a recent decision in Arizona concerning a 403(b) tax-deferred annuity plan that involves employee money sent through salary reduction to annuities issued by a number of commercial companies, as well as by TIAA-CREF. That decision, at the U. S. District Court level, was that the plan is illegal because all of the insurers use sex distinct tables. This is despite

the [illegible]at all of them provide a lump-sum option.

Well, we could go into how much effect the proposed change will have on the various options: no effect on the most popular joint-life options, and a range of impact from 1% to as high as 8% for one option — the single life annuity, which has no guarantees for any survivor; i.e., the straight life annuity where all payments stop when the annuitant dies.

No insurance companies have yet constructed merged-gender tables, but the shock waves are still running through the insurance industry. But they too will be affected by this if the government's position is indeed the wave of the future. If they want to continue to provide tax-deferred annuities and annuities for pension plans, they will have to issue merged-gender annuities in the future.

You've probably heard something about the court-ordered settlement discussions we've gotten into with the EEOC. This was an attempt to see if a global settlement of this complex issue couldn't be reached out of court, and [illegible]ave been in a number of meetings with the [illegible] that issue. The main remaining issue is re[illegible]ivity. We've agreed to adopt "unisex" for future premiums, if permitted by state insurance laws, so the main question is retroactivity; that is, whether benefits resulting from past premiums are going to have to be "equalized" and if so how. There was some movement during these discussions, but very little really. We offered to move toward them a little bit. They moved the other way. It was not a productive settlement discussion, and there won't be any settlement. We're poles apart. But there was some increased understanding of each other's position, which we think will be helpful in ultimately getting a decision on retroactivity

in the courts.

Now the EEOC's position, as we read it, is that the merged-gender mortality table should be used not just for future premiums, but to determine total benefits for all people who retire in the future, which means benefits resulting from all past premiums as well as from all future premiums. You see, they contend that TIAA dividends, over and above the 3% contractual guarantee, and all CREF earnings are fungible and therefore not committed to any individual. They contend that we would be fully justified in shifting those earnings around among participants in order to "unisex" benefits resulting from past premiums. In other words, all TIAA dividends over the minimum guarantee and all CREF earnings should, in their view, be available, as needed, for that purpose. We also understand that the EEOC is going to seek some kind of back pay award for women already retired as well as future benefit increases for them.

Our position, and that of many of our participants who express them- selves in no uncertain terms, continues to be that all benefits that are attributable to past premiums should continue to be determined according to the representations that we at TIAA-CREF (like all insurers) made when the premiums were paid, and in all the years since: that in retirement those benefits would be paid out to men on the basis of male life expectancy and to females on the basis of female life expectancy. We don't think we have any legal or moral right to change from those representations. However, everyone is aware that if ultimately the Supreme Court says you have to do it, then that will be the law of the land. But we don't see it as the law of the land now, and we think that men would be justified in suing us if we did it, so to speak, voluntarily as to past contributions.

So we'll continue to oppose the shifting around among participants of investment earnings on past accumulations in order to unisex benefits from past service. And of course we oppose any position that would impose financial liability on our participating institutions. And we and the EEOC now expect litigation on the retroactivity issue to work its way up to the Supreme Court. We think we and our institutions have a very strong good faith defense on retroactivity. Not only do state insurance laws authorize sex-distinct tables; even at the federal level there are guidelines that still say it's okay to provide actuarially equal benefits for men and women instead of equal monthly benefits. And the Manhart decision was very bearish toward any retroactivity where conflicts in government rules have not been resolved.

My last message on this subject is that there has been significant progress on implementing merged-gender tables for future premiums. There will be a letter on this going out to you next week, hopefully. You'll remember that we had planned to put this table in earlier but we held off. If you got my July 22 letter you know why. We deferred because at that time the EEOC said they would press charges against all 3,400 institutions and TIAA-CREF, alleging that our proposed use of merged-gender tables for future premiums would be a violation of Title VII. Since they were clearly ready to bring those charges against all of your colleges, we held back, and although our discussions with them didn't end in settlement, we made some progress toward implementation of merged-gender tables for future premiums that does meet with EEOC approval. They have agreed, at our urging, to separate the prospective and the retroactive issues so that we can go ahead on the prospective basis. And we agreed to make some changes in the merged-gender amendments in order to achieve EEOC approval.

The EEOC is issuing an Opinion stating that adoption of the new table for future premiums will not be a violation of Title VII or the Equal Pay Act, either by TIAA-CREF or by any of our participating institutions. So the way is clear to go ahead again, but it means another round of seeking state insurance department approvals, because the amendment form has been changed.

The EEOC's Office of General Counsel has written a letter for the insurance departments, stating that using this rate schedule, and I quote, "will afford full protection to TIAA and all participating institutions against all claims of sex discrimination by reason of the payment or receipt of premiums or benefits under the new rate table." So they've cleared that, and we must now seek the necessary state approvals. If we get them, we will send out the amendments.

But the retroactivity issue remains, and the legal staff of the EEOC has informed us that they can no longer, will no longer defer the nationwide charges dealing with the retroactivity issue. Although we are trying to stop it, the EEOC is apparently going ahead with this redundant charge, against all 3,400 institutions individually, and against us, despite the fact that the basic issue is already being contested in nine separate U. S. District Courts. We don't know the specifics of this extreme measure and we don't know the procedures that are going to be established for responding to it. The EEOC will probably seek to consolidate all of it into one court case in the Southern District of New York. That seems to be what they want, and it would certainly be what we want if there is to be a national charge -- to get it into one court case instead of many. We'll keep your institutions informed about these developments as they occur. The American Council on Education has announced to its constituency that it has hired outside counsel to offer guidance on

how to respond to these charges if they come out.

So, in summary, we expect to be going ahead with the merged-gender table for future premiums if the state insurance departments approve, and we're going to carry the retroactivity issue all the way to the Supreme Court. It's one thing to change the rules of the game before the game starts, but it's quite another thing to change the rules of the game and its score when the game is over. However, if the Supreme Court ultimately says do it, we will do it, and so will everyone else, and it will become the law of the land, retroactively. If we lose on the retroactivity issue, that is, if all benefits to people retiring in the future must be on a unisex basis, my judgment would be that this would not be a charge to the colleges. Rather, it would be a charge to the men through the method now proposed by the EEOC; that is, through shifting earnings on past accumulations among participants in order to unisex retroactively.

Q. How will the change for future premiums affect the men?

A. The Bulletin we'll be sending to people when we make the change has a whole list of the differentials to men. For example, with the most popular joint-life options, which are chosen by 60% of the men, it will make no difference at all because there is already a male and female in the couple, normally. On the other options, the one-life options, there will be a difference. The biggest difference is where a man elects a benefit only for his life with no benefits for a survivor, the single life annuity, so-called. If he builds in a ten or twenty-year guarantee, so that payments are guaranteed even if

he doesn't live for the ten or twenty years, the difference is much less, because for the first ten or twenty years no life contingencies are involved. Also, of course, the proposed change affects only future premiums, so it would make more of a difference to you because you're young. But for people who've been in the system for a while it would make less difference because it affects only those premiums paid between now and the time they retire.

Q. Will this affect tax-deferred annuity plans as well as pension plans? And other insurers too?

A. Yes, the whole thing. Because both types of plan are considered "employer sponsored retirement plans," whether they're with TIAA or anyone else.

Q. Who are the defendants in the present cases?

A. Right now the nine court cases are against TIAA-CREF and, in each case, a college or university.

Q. How much would retroactivity cost?

A. Well, that would be the cost to the men, and it would depend on what options the men elect. It's not something you can know in advance, but if you tried to fund it today, it would be a very big tab. But over any one man's life expectancy it will be either 0% for him or up to as high as 8% depending on which option he elects and how much of his income will come from future premiums. As I've said, we feel we have no right to go unisex for

past premiums when we have been assuring people, as everybody else, that those premiums would provide benefits based on sex distinct tables.

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TIAA/CREF and Planning for Retirement

Donald S. Willard

Mr. Willard, a Harvard Business School alumnus, has had a career which has included service as a [illegible] academic administrator and service [illegible] in the insurance industry. He is [illegible]tly the Executive Vice-President of TIAA.

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Two things have happened today that directly affect me. First John Biggs has done a very good job of telling you what I was going to tell you, and secondly, in the interest of time, I've been asked to try to truncate my remarks. This reminds me of the epitaph on Robert Burns' gravestone which says, "I knew if I hung around long enough something like this would happen to me."

I have two things that I want to talk very briefly about. First, as Tom has indicated, I want to talk about some pre-retirement counseling, or pre-retirement planning programs that are taking place in higher education. As some of you may know, back in 1977 we did a pretty intensive survey of retirement planning programs in higher education. The results were published in a book called Retirement Preparation in Higher Education, by Jim Mulanaphy, who is one of our research officers. For those of you who have not seen it and are interested in this subject, you might like to request a copy. That study showed that, out of 2210 responding institutions, 96, or about 4%, had pre-retirement planning programs. Now, since that time, in a very short period of two or three years, there's been a growing interest in these programs. As this interest has developed, our participation in them has increased substantially. The programs

take a wide range of forms, from multi-session programs that cover a whole variety of topics, to single programs that concentrate solely on financial planning. Our role in these programs is in the fin- ancial planning sessions. We partici- pate in such sessions at a good many institutions by sending a TIAA-CREF representative or two. Generally a representative from the Social Security Office from that region also participates. Together we discuss financial planning as it applies to TIAA-CREF and Social Security. These have been very interesting and I think very worthwhile sessions.

The most interesting and exciting program so far as we are concerned is a new pilot program that we instituted this fall. We refer to it as our Community Program. There are a great many institutions around the country that have a very small number of people on their staffs that are 55 and older that are concerned about retirement. It's not feasible for us to arrange financial planning sessions at such institutions. So what we do is schedule programs in urban centers around the country and invite employees age 55 and over from institutions within a 50-mile radius to come and spend a half day with representatives from TIAA-CREF. Generally, here too, a representative from the Regional Social Security Office is in attendance. Indeed, for the last three days we have been running one of these Community Programs right here in Providence, and some of you may be aware of them. We are doing this, of course, with the cooperation of the institutions located within a 50-mile radius. These programs have been very well received. We've also just completed a series of such programs in Rochester where we had, in the course of three or four days, some 600 people attend. It may interest you to know that we have 30 of them already scheduled for 1981 and we will probably be holding well over 50 by the time 1981 is over. So if you're interested in knowing where

any of these programs are being held, we'll be glad to check the schedule and let you know.

I'll just pass by that subject now and go on to the other topic that Tom mentioned -- ways that employers and employees and pension systems are trying to cope with inflation. I'm going to hurry along and just try to hit the high spots, starting with the employers. What are they doing to cope with inflation occurring before retirement with respect to their pension plans? Well, they're doing several things. One thing is a pretty simple approach. It's simply to increase their plan contributions. The idea here is to provide a cushion, if you will, for the person entering retirement. This would give the person some flexibilities that John McCormack spoke about earlier this morning. Funds that are above a retired person's expectations could be used in a variety of ways in order to offset the ravages of inflation. It's not a big thing, but it is something that a number of institutions have done.

Another approach that a few institutions have adopted is what we call a combination plan. This is simply a TIAA-CREF defined contribution plan, with contributions of 10, 12, or 15% of salary, coupled with a floor or guaranteed benefit. The plan provides that the retirement benefit will be the larger of the benefit resulting from the defined contributions or the benefit guarantee. Now if the benefit guarantee is greater than the benefits generated by the defined contribution, then the institution supplements for the difference. For example, a combination plan might have a floor benefit for a career employee of 50% of final average salary, including primary Social Security benefits. If the contributions under the plan don't produce a benefit equal to 50%, then the institution provides a supplement.

I should have said up front that some of these

things that I'm talking about may have ERISA implications. But I want to talk concepts -- I really don't want to get into specifics. There may be some problems that have to be worked out. But, hopefully, they can be worked out in one form or another. We'd rather approach this from a positive standpoint knowing that there may be problems to overcome. First let's find out what an institution really wants to accomplish or try to do, and work towards that objective and hopefully work over, around, or under the problems as best we can as we go along. I should add, and perhaps this isn't necessary, that if the institution does adopt the combination approach, it takes on an added commitment. In other words, their pension commitment does not stop with the payment of that defined contribution as it does under pure or defined contribution plans, because they've taken on a commitment to supplement those benefits, if necessary, in order to bring them up to the floor guarantee.

Now, what about coping with inflation during retirement? The most popular way, at least in the private sector, is for employers to make ad hoc adjustments, which ERISA defines as "gratuitous payments". Arrangements of this kind take many forms. They are either a flat dollar amount of supplement, a fixed percentage amount, or a percentage that varies determined by formula, cranking in such things as years of service, age, amount of initial annuity income, years in retirement, years since any last or former increase might have been made, changes in the CPI, and so on. The choice of the arrangement depends upon a number of things -- the cost and funding implications, the original level of the pension, changes in the cost of living, changes in Social Security benefits, changes in CREF, and so on. But the ad hoc approach has been most popular, basically because it gives the employer a better control over costs; the employer is not committed to any

on-going arrangement, the amount can be varied, up or down, from year to year, or it can be omitted in any given year. The employer has control over the timing, as well as the amount, and indeed, if Social Security benefits increase or CREF benefits take a big jump, the amount can be varied to take that into account.

In the public sector, as most of you are aware, the approach that has been taken through employers and their public retirement systems has been the indexed approach, or the automatic increasing benefit approach. You know, I'm sure, that the federal programs -- the Civil Service Retirement System, the Uniformed Services System, and Social Security -- index fully to changes in the CPI. At the state level, retirement systems for public employees and teachers that index benefits generally cap them at a 3% level for the most part, but some of them go as high as 5%. Or they go the automatic route; for example, they increase benefits automatically 3% a year without regard to what happens to the cost of living. John Biggs has already alluded to the concern in the private sector over this approach because of the cost, and indeed it is a concern. Employers are wary of the cost of any kind of a commitment to a continuing and unknown increasing benefit. There are also some conceptual problems with that approach, but I won't take the time to get into them.

What about coping with inflation before and during retirement? John Biggs addressed that question eloquently in terms of what employers and of course individual participants are doing through a variable annuity based on investments in common stocks. As John indicated, for the first 20 years or so after the development of variable annuities in 1952, equities performed very well. They performed beyond most people's expectations. Then there were a few years in the 70's when equities

were very disappointing, particularly to people who were in retirement and experiencing a decrease in their variable annuity benefits in a period of rising living costs. In the last few years equity performance has turned around. It's not been an unbroken line upwards, but since the middle of the 1970's common stock performance has been quite good indeed. Many knowledgeable people who are making (I was going to say "foolish enough to make") predictions of what's going to happen in the future, think that the decade ahead is going to be a very good decade for equities. I'm talking about people, many from COFHE institutions, like Burt Malkiel at Princeton and Modigliani at MIT and Jim Tobin at Yale. You may have read a recent article where all three of these people were bullish about equities. I think it was in the last issue of Business Week magazine.

Now, there's also a strong feeling that the employer should not take full responsibility for providing some kind of hedge against inflation, that the individual should play a role in this. And many of them indeed are doing just that. They're doing it in all kinds of ways: through personal savings vehicles of one kind or another. And, as I'm sure many of you know, one of the most popular vehicles being used these days is the tax deferred annuity, because of its tax advantages and the flexibility that it has. At TIAA alone, there are some 94-96,000 people who are putting extra contributions into Supplemental Retirement Annuity (SRA) contracts. That's just people putting aside extra funds through TIAA-CREF. There are many, many more who are doing it through the products of other insurance companies. It gives them a good deal of flexibility, particularly in the early years of retirement in terms of how they want to handle their finances. They can defer part of their regular TIAA-CREF income while drawing income from their SRA, or vice-versa, or they can start their TIAA income but defer begin-

ning their CREF income to a later date. Indeed, an individual has as many as three starting dates in TIAA and three starting dates in CREF if they want to use them.

Finally, I'd like to talk just a couple of minutes on two approaches to cope with inflation that are under consideration at TIAA-CREF. One of them is the Kemeny approach that John McCormack went into in some detail. We've been working with Dartmouth College, providing them figures on this, talking with them about the approach and how it would work. I won't say anything more than that because John covered it pretty thoroughly. It's controversial as many things are, but for the concern that John Kemeny expressed, it may be an acceptable alternative for some people. He's worried about the person who says, "Hey, look, I can cut it for the first ten years or so. I've got enough set aside. I'm not too worried about that, but what am I going to do when I get to the end of that ten year period? Where am I going to turn for help?" This is what's behind the Kemeny approach of nothing for ten years in the way of a supplement, then a good infusion of money, perhaps followed with an increasing annual benefit thereafter.

The other approach Tom alluded to in his introductory remarks is very close to the increasing annuity John Biggs is suggesting. The initial TIAA income would be based on a 4% assumed interest rate resulting in an initially lower total income than if it had been based on the full pay-out dividend rate. Then each year in retirement any pay-out dividend interest in excess of 4% would be used to finance an increase in the annuity income. If the full pay-out rate (contractual plus dividends) were 10%, for example, 6% interest on the reserve, or present value, of the annuity would be used to finance the next increase, in effect, a "dividend addition" purchasing an

additional lifetime annuity.

Alternatively, another method being considered would offer the retiring participant a reduction in both the contractual and dividend portion of the initial TIAA income. The reduction amount would be used to finance a pre-selected rate of increase each year of, say, 3% or 6% in both the contractual and dividend portions. For example, if a 6% increasing benefit was selected, the contractual amount would be guaranteed to increase by 6%, each year, no matter what happened to interest rates. The dividend amount would increase by 6% a year as long as the dividend scale in effect at time of retirement remained unchanged. When TIAA's payout dividend rate changed, say from 10% to 11% or 9%, the overall level of dividends would change accordingly, but the yearly 6% interest factor would still be applied to whatever dividends were payable.

Those are the things we're working on now. We've got a ways to go yet. It takes a lot of changes internally in operations and systems programming, writing material, getting all our ducks in a row, and so on! But some approach to an increasing benefit option is the thing that's very much on our minds these days and on the drawing boards at TIAA-CREF.

I'll make just one final comment. I was pleased to hear John Biggs say that when a company is involved in a controversy that is as complex and involved as the unisex issue, it takes up a lot of time. There is a lot of work involved in making a conversion to unisex rates, and there are only so many people and so many machines to do so many things. So, we have to limit our options and we have to be very careful in setting our priorities. I assure you that the increasing benefit option is right up there at the top of the priority list with the unisex issue.

ADEA Implications for TIAA/CREF Retirement Plans

John J. McCormack, Jr.

Mr. McCormack is a senior vice president of TIAA. He heads the Institutional Counseling Division and has extensive experience in the design and implementation of retirement plans.

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Yesterday we heard a good deal about ADEA and its regulations from Laura Ford. I'm going to [illegible] a few comments, hopeully expand on Laura's comm[illegible] a little bit. Laura mentioned that on July 1 of 1979 the administration of the Age Discrimination and Employment Act switched from the Labor Department to the EEOC. Just prior to that switch, and it's not uncommon for these kinds of things to happen, the Labor Department promulgated its regulations or, as it is officially called, an interpretative bulletin on how the amendments to the Age Act would affect employee benefit plans. Under the DOL interpretative bulletin which, by the way, is still in effect, defined contribution plans -- the TIAA-CREF type plans -- can cease contributions for individuals who continue to work once they reach the normal retirement age. Defined benefit plans - typical industry plans - currently are not required to credit salary or service for employment after an individual reaches the normal retirement age.

Well, shortly after that shift in responsibility on July 1 of 1979, the EEOC became concerned about "windfalls" that they saw accruing to sponsors of defined benefit plans. Under defined benefit plans, as I just mentioned, employers are not required to count salary or service after the normal retirement age even though individuals have

the right to work beyond that age. This windfall that the EEOC saw accruing results from the fact that there are actuarial gains and earnings gains accruing when individuals delay receipt of their retirement benefits. John Biggs touched on how the accruals occur. Mortality concepts and their implications for pension plans have been discussed a lot over the last day and a half so I think you can understand that if a person delays receipt of benefits, the liability for the payment of retirement income is shorter; therefore, if the benefits are frozen as of the date the individual reaches normal retirement age but he takes those benefits four or five years later, they are going to be less expensive to purchase when benefits actually begin four or five years later. What the EEOC saw in this windfall to employers was a loss to individual participants and a potential for a charge of age discrimination because older employees who continued to work are not receiving pension credits for salary and service after attainment of the normal retirement age. Well, the EEOC proposed to correct this problem in a rather strange way that may have some of you confused. A number of people have said to me - didn't the EEOC come out with regulations that change the Department of Labor regulations? The fact of the matter is no, they have not come out officially with any changes in the regulations on the amendments to the Age Discrimination Act. There is a requirement that the regulatory agencies share in draft form the proposed regulations they are considering, and the inter-agency draft of the EEOC proposed regs on ADEA is what has been published in a number of places but not officially released in the Federal Register. In the last couple of months I have had calls from at least three institutions who thought the EEOC had come out with revised regulations. It's quite obvious when you read the EEOC regs that the date for comments, which all proposed regulations include, is blank. So you can see very quickly in the first couple of paragraphs

that they had not been officially released but were floated or leaked for public reaction and, needless to say, they have gotten a lot of reaction.

Well, to correct this windfall occurring to sponsors of defined benefit plans, the EEOC proposed:

That defined benefit plans credit years of service and salary for employees who continue to work beyond the normal retirement age or credit the actuarial and earnings gains.

In addition, they also took the opportunity to propose a change in the regulations for defined contribution plans:

The EEOC would require continuation of contributions for an employee unless a stated benefit objective was achieved when the employee reached the normal retirement age.

Defined contribution plans usually use a benefit objective they would like to achieve for a career employee at the normal retirement age in order to set the rate of contribution under the plan. However, this benefit is not guaranteed and may be more or less depending upon years of participation in the plan and the individual's salary history. If a benefit objective is required, it would become a formal part of the plan and a commitment for the institution that they do not currently have.

Since defined contribution plans do credit the actuarial and earnings gains to individuals who delay receipt of their benefits which, in some cases, I guess has been viewed as something of an incentive to stay on, it's important to note that this practice may also save defined contribution plans from being required to put a stated benefit

objective in the plan. Since we do credit the actuarial and earnings gains to individuals, we already meet one of the proposed requirements the EEOC is proposing for defined benefit plans. We're also encouraging the EEOC to recognize this fact and not require contributions beyond the normal retirement age or require a stated benefit objective. If an individual delays receipt of his benefits, each year he delays the receipt of the benefits beyond age 65 they will increase by at least 10% a year. Well, as I say, we have encouraged and suggested to the EEOC that they recognize this fact which they did not appear to be aware of, and they indicated they would take our suggestions under consideration. I make no guarantees because I don't know where they'll come out. I think the EEOC is waiting for the election results before going public with revised ADEA regulations. I would mention that any revised regs will be proposed. There will be a comment period followed by final regulations. So, it will be a matter of time before anything happens on this issue. The EEOC commissioner's meet every Tuesday and the last time I talked to the EEOC, they anticipated that the amended regulations would be on the agenda for the commissioners' meeting on the 7th of October, and that's obviously past. I did hear that last week it was on the agenda as the fourth or fifth item, and just prior to the meeting it was pulled, which may signal a variety of things - is there concern about the floated regs among the other agencies? is there concern about the election? is there concern about how the regs have been structured and whether or not they are fair and equitable? It would be speculation on my part to try and tell you why they were pulled from the agenda, but they were.

The 1978 Amendments to the Age Act increased the mandatory retirement age from 65 to 70 and there was some concern on the part of our participating institutions about whether or not employers

with TIAA-CREF defined contribution plans should continue contributions between the ages of 65 and 70 and if so, should they reduce those contributions because they will be making them for five years longer than they had originally anticipated? Well, I thought it would be interesting to report on what has actually happened since the amendment to the Age Discrimination Act. The great majority of TIAA and CREF retirement plans have not changed their normal retirement age from 65 to 70, and to keep retirement financially possible for individuals who want to or should retire before 70, virtually all of the plans have also kept their pre-DEA amendment rate of contribution. In 1977, there were 65.4% of all TIAA participants in retirement plans with the normal retirement age of 65. In 1980, 74.3% of all of our participants were in retirement plans with the normal retirement age of 65. The number of participants covered by plans with the normal retirement age of 65 has increased from 1977 to 1980. In addition, for staff members employed beyond the normal retirement age, that's beyond the age of 65 in most cases, 75% of our programs continue contributions to age 70 or to retirement. The balance cease contributions at the normal retirement age. In spite of the changes in the mandatory retirement laws, improving health and increasing concerns about inflation, approximately 52% of the TIAA-CREF participants beginning annuity income start payments at or about age 65. Of those who start their income after age 55, some 27% begin their payments before age 64. This is compared to about 17% in 1972. The percentage starting annuity income at age 67 and above has declined from 33% in 1972 to 21% in 1979. Although individuals now have the option of continuing to work beyond the normal retirement age, between the ages of 65 and 70, we have not identified internally any trend towards annuity incomes starting at the older ages.

Well, you all know that the amendments to the

Age Discrimination Act provided a special exemption for tenured staff members and it allowed institutions that had tenured individuals to have mandatory retirement at age 65 or the normal retirement age up until July 1, 1982. Our data indicates, that about 11% of the colleges and universities with the TIAA-CREF plans are retaining early mandatory retirement provisions for tenured staff members. Roughly 76% now have age 70 mandatory retirement for all employees including tenured staff, and believe it or not, 13% have no mandatory retirement age whatsoever. That's basically what I was going to cover on ADEA.

Comments

Robert Link

Mr. Link, a Yale Alumnus, has recently retired from a career in the life insurance industry. He has extensive experience with private pension, group insurance and, as Vice President of the Equitable Life Assurance Society of the United States, corporate management. Mr. Link now plans to launch a second career as an independent consultant.

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I've enjoyed this meeting tremendously. It makes a big difference to be here, to hear what people say, and to get some of the feeling contained in these issues. You don't quite get that feeling from the executive summary of the studies that have been done, and the feeling is very interesting.

I'm reminded of Murphy's Law. You know the first Murphy's Law: if anything can go wrong, it will. There's a whole series of them. One says if there are several things that can go wrong, they all will go wrong, and they'll do it at the same time and in the same direction.

I think that characterizes the problem that this meeting is concerned with: First, we have an unbalanced faculty population, so that retirement is more of an issue than it would be normally or than it has been in the past. Second, we suddenly have roaring inflation creating great fears about retirement. And third, we have the age 70 thing suddenly upon us. All of this happened at once, just as Murphy said it would.

I really think though, all of this and the problems that this meeting is discussing are symptomatic of a deeper problem. I've heard about it during this meeting. I'll speak now from the deep well of my ignorance about academia, but this is how I see it. The real issue that I've heard repeatedly is, how do we avoid paying $30,000 when $16,000 would probably get us a better product?

This is a classic business problem. In the private or profit-making sector, they have tools to deal with the problem. They have the legal and moral right to prune staff. In varying degrees they practice this art. It's a very difficult art to practice, but they do it. But, what I am hearing here is that in academia, particularly with respect to the tenured faculty, you don't seem to have the tools or the moral or legal right. I'm also hearing little feelings or comments that may be you're glad that you don't, because if you did it would be so difficult to exercise those rights and make the heart-rending discriminations that are necessary to do it right.

All of this leads me to a suggestion. You have discussed some ways of encouraging early retirement of tenured faculty. These devices cost considerable money, at least if you assume some retirements would have taken place anyway. Suggestion: Put these devices into effect on a basis such that they can be withdrawn again if circumstances change. Couple this with a resolution to address those aspects of the tenure system that stand in the way of more creative staff pruning. If I've given enough offense, I'll remark on a few things that have cropped up during the program.

John Biggs talked about the Consumer Price Index being an inappropriate measure of inflation. I passionately agree. There are a number of things. First is the treatment of taxes. Payroll

taxes are in the CPI. If there were value added taxes, they would be. Many other forms of taxes aren't. This leads people to say that payroll taxes are inflationary and income taxes aren't. That's hogwash. That's a defect in the CPI.

Secondly there are other things in the CPI that one could question. This is less a scientific question than a question of purpose, especially because the CPI is used to adjust the income of government employees, Social Security beneficiaries, and people with labor contracts. To the extent that expenses are incurred and prices are raised by complying with government regulations for environmental and consumer protection, the unindexed people are paying for the indexed people's share of these added costs. It would be great if there were a way to recognize that. Third, John Biggs mentioned improvements in the quality of things. Classic examples are tires rolling further and razor blades giving more shaves. I've read articles by economists alleging that you've got 2% right there. And fourth, there's the housing thing.

I've corresponded with Commissioner of Labor Statistics Janet Norwood, and I've also written letters to a few Congressmen and Senators. I see very little sign that the government is interested in pursuing these matters.

John Biggs mentioned the indexing of private pension plans and suggested that this is not an absolutely hopeless area. I think he's right. The fact is that the sponsors of those plans have been spending the inflation bonus in their investment earnings on either increasing nominal benefits or reducing their own costs. They have painted themselves into a corner. But if there's enough time, maybe they can get out of it.

I am charmed by John's major proposal and by

the studies going forward at TIAA. Perhaps out of these studies will come something that will help a person who doesn't want to spend the inflation premium up front but wants instead to let it come through with a timing that fits his need.

The National Commission on Social Security has recently done a survey. It covered about 1600 families, various ages, income levels, and so forth, supposedly representative. This is in support of their charter to study the whole issue of Social Security in this country. It's interesting that some of the attitudes revealed in this survey correspond to attitudes revealed in the COFHE study. This is particularly the case with respect to people who intend to retire late or intend to retire early, how they relish the thought of retirement, and how they fear the economic consequences. The same attitudes were found.

Next I'd like to mention a short piece by one Carter Henderson. He is a writer and lecturer on financial matters. With his permission, I'll quote in part: "Not too long ago, after lecturing on the economic outlook at a Southern university, I had occasion to chat with two women: the first an affluent college professor with extensive investments who was visibly frightened by the future, and the second a younger woman with no financial assets who was looking forward to it with confidence and anticipation." He talks about the incongruousness of that situation and explains that the college professor was concerned because of the disinte- gration of the economy with which she had been familiar, and then he went on to say, "Since it will take years to conquer high-level inflation if we're lucky (and decades if we are not), millions of investors, myself among them, are turning to a fail-safe investment strategy -- unknown to Wall Street or the Gnomes of Zurich -- which can substantially increase their economic

security as the nation enters a New Age of waning material affluence. New age investors see the United States at the beginning of a great economic transformation, [etc. etc. and they] are taking command of their own economic destinies by reducing their need for cash incomes, learning to coax more purchasing power out of the money they do have to spend, becoming do-it-yourself experts, capitalizing on the untapped productive power of their homes and communities," and so forth.

Well, it's an interesting concept. I once had lunch with Mrs. Henderson, who is a practicing futurist and making money at it. They are living this way. She described some things she and her husband are doing. In this culture you don't boast about how much your possessions cost; you boast about how little they cost after you have bought them in a junk yard and fixed them up. You grow your own food. Very interestingly, the Hendersons are going bare on medical coverage. They say they don't want to be in the system; they'll do it themselves. They find as a consequence their attitude towards the subject of health is quite different from what it would otherwise be. They are very positive about staying healthy. Aerobic exercise, the right kinds of food, and such.

If your're going to do this kind of thing, you have to plan for it. In my own future life I hope I can succeed to some degree in living this way. Over my lifetime I have developed a few of the skills that are necessary. I suspect it's best to start young on retirement planning, on learning and on developing the skills and interests that will permit you to make that transition with relish and enjoyment, doing things for yourself instead of depending so heavily on money.

People will argue endlessly about details and specifics. What I mean to suggest here that we

need a much more comprehensive, creative, and per-
sonally long-term view of what retirement is all
about.

Faculty: Planning for Retirement

Aaron Lemonick

Aaron Lemonick is Dean of Faculty at Princeton University. He has served as an active member of the COFHE Retirement Study Advisory Group and was instrumental in the planning of this conference.

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I have been asked to moderate this last session. My task is to get it started, to introduce the speakers, and to bring it to an end at the time promised.

I think it appropriate at this point to say a word of appreciation for the conference and the work that went before. The 1978 amendment to the Age Discrimination in Employment Act, which established 70 as the earliest permissible mandatory retirement age presented the institutions represented here, not to speak of all the others, with a set of problems, many of them common. Not the least among these problems was the fact that there was a startling lack of information -- we did not singly or collectively really know the facts of our situation, what the effects of the newly raised retirement age would turn out to be, what might be done about it. It is a tribute to COFHE that it recognized the need and set out to do something about it. It is a tribute to Colin Campbell who gave leadership to the task over the past two and a half years that the task was accomplished. This conference is a capstone of that effort.

Before going on let me voice some thanks on behalf of all of us to some of the people who made this conference what it has been. First of all, Frank Durand, Maurice Glicksman, and Brown University for hosting this conference in the

effective way that a conference ought to be hosted; thanks go to Reiner Summer the manager of this Club and Betsey Wallace who is in charge of preparation and serving of the food for the style in which we have been received. I'm sorry that Jack Sawyer of the Mellon Foundation is already gone. Without it and its support there could have been no reports and no conference. The Foundation, its directors and its officers, were sensible and sensitive and thoughtful, and responded to a felt need, a need which has been met in such felicitous a way. I think it also in order to thank the speakers at this conference, and all the participants for the most focused and interesting conference that I have the privilege to attend for a very long time. Finally I think that we ought to thank again the Board of COFHE which recognized the need and Colin Campbell, Kay Hansen, Eve Pratt, and Carol Finney, without whom none of it could have occurred. COFHE's effort has been an important one.

In sailor's parlance, if age 70 is a full gale, then certainly uncapping would be a hurricane, and to pursue the analogy, and the inflation adds a disturbed, confused, steep, breaking sea to the danger. As institutions we are all in it alone, but we're all in it together. At the end of this session I would like to save some time to open it up to you the participants to get your thoughts as to what you see that now needs to be done by this most effective group.

We have two speakers this afternoon. They will not be speaking to pensions as such, nor rate schemes, nor slopes, nor ramps, nor other things which have already been mentioned, they will be speaking about the individual with whom we are all concerned, the faculty member. One will speak about the opinion survey which sought to find out what the individual faculty member thought about his or her own retirement, his or her own work, his or

her own retirement date, and the possibility of early retirement. Early in the effort it was recognized that this information -- what the faculty member felt — was an important element in any attempt to meet the problem. It turned out that we had a very important asset, the Crowell University Professor of Social Sciences at Wesleyan, Herb Hyman the man who was not only the liaison person with the Institute for Research of Social Behavior which did the opinion survey, but was also the person who translated our fears and hopes and dreams about the opinion survey to the Institute in such a way as to assist them to construct a survey which not only got a 75% response, an amazing response but also taught us something and from which one could draw conclusions. I would like to introduce to you now, Janice Clinthorne who will speak about the "opinions" as they relate to the issues of this conference.

COFHE FACULTY RETIREMENT PLANS

Janice Clinthorne

Ms. Clinthorne, who is an analyst with the Institute for Research in Social Behavior, was the Project Director for the COFHE study. Her professional background combines research and consumer economics. She has served on the staff of the Community Council of Greater New York.

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In Fall, 1979 the Institute for Research in Social Behavior conducted a mail survey of over 1600 faculty at COFHE institutions, asking about their plans for retirement and about various circumstances that presumably influence retirement decisions, such as health, job satisfaction, and financial status. We were particularly interested in how the new law on the mandatory retirement age may affect the retirement plans of the older faculty.

Twenty-six of the 30 COFHE institutions participated in the survey. Our probability-based sample was selected to represent only those faculty who were tenured, 40 years of age and older, and teaching in the arts and sciences faculties.

The faculty were quite cooperative -- 74 percent returned completed questionarires -- an extremely high response rate for a mail survey. A comparison of the responders and nonresponders indicated that these groups did not vary greatly on age, sex, rank and academic discipline. The only notable difference was that the nonresponders tended to cluster somewhat at Ivy league schools.

Expectations About Retirement

The very first question we asked faculty was about their general attitude toward the prospect of retirement. About one-third reported that they look forward to retirement. A smaller proportion -- one-fifth -- actually dislike the prospect of retirement, and the rest are either neutral or uncertain about it.

Women, incidentally, were somewhat more likely to regard retirement in a favorable light. Overall 40 percent of the women look forward to retirement, compared to 31 percent of the men.

Later in the questionnaire we asked faculty 50 and older about specific hopes they might have for their own retirement. We listed a variety of favorable retirement prospects and asked them to rate how much they looked forward to each of them. The most popular prospects were:

1. Doing writing and research in their own field that they do not have enough time to do now (79% reported they look forward to this "very much" or "quite a bit").

2. Pursuing hobbies, arts, crafts, music, languages and other personal interests (66%)

3. Spending more time with their families (59%).

Just as they were more inclined to report a favorable attitude toward retirement in general, women were also more likely than men to look forward to these specific retirement prospects.

We also listed some common worries about retirement. These covered a wide range from financial worries to concern about physical deterioration, loneliness, boredom, and so on. Only one worry was mentioned by a majority of

faculty — the fear of not having enough money after retirement. Sixty percent of those 50 and older reported this was something they feared "very much" or "quite a bit." The next most common worry also reflected a concern with future financial status. About one out of four reported they were worried about having to find another job to supplement their income after they retired. Smaller minorities (21 to 14%) reported they were worried about other unfavorable prospects such as loss of prestige, loneliness, boredom, or feeling obsolete.

Knowledge About Retirement Policies

How well informed are faculty about their school's retirement policies? The great majority (82%) already knew what their school's current mandatory retirement age was, but they were less informed about their school's policies on early retirement. Among those 55 and over, 40 percent did not know whether or not their school had any policy on early retirement. Those at universities were the least informed about early retirement policies — 48 percent did not know whether such plans existed at their university, compared to 35 percent of those who taught at small colleges, women's colleges and Ivy schools. And faculty are even less informed about the availability of pre-retirement counseling. Fifty percent of those 55 and older did not know whether or not their school offered any such counseling.

Retirement Intentions

Perhaps the key question in this study was, given the choice of remaining until 70, how many plan to do so? Not all the faculty do, in fact, have this choice. A small group of older faculty members will reach the mandatory retirement age at their schools before the new law takes effect. They may or may not have the choice

of staying on, depending on whether or not further changes are enacted by their state legislatures or their administrations. Because these uncertainties make their retirement plans more problematic than those of other faculty, we excluded these persons from the main analyses of retirement intentions, the results of which I am presenting today.

After making sure that respondents understood the implications of the new law, we asked them at what age they expected to retire. We asked them to answer this "realistically, taking everything into account (including the things you can't control)". The data show that for every age group, including the very oldest, the majority expect to retire voluntarily before age 70.

For example, 46 percent of those 61 and older expect to retire at age 70. The average expected retirement age for these faculty is 68.2 years. Among those 55-60, only 38 percent expect to stay on as long as age 70, and their average expected retirement age is 67.3 years. In general, younger faculty are more likely to plan voluntary retirement than older faculty. This partly reflects the fact that the ranks of the older faculty have been thinned by the absence of those who have already taken early retirement. Still, there does appear to be a clear relation between current age and expected age of retirement -- the older the faculty member is, the more likely he or she is to plan to stay until age 70. This suggests that younger faculty in their forties, for whom retirement is relatively far off, may be more influenced by their preferences, and that older faculty, for whom retirement is an imminent decision, are more influenced by the realities of current economic condi- tions, particularly inflation. However, even among the oldest -- those 61 and older -- 19 percent expect to retire at 65 or earlier. And the oldest faculty presumably have made the firmest

plans since they are most likely to have given serious thought to their retirement plans and to have taken some practical steps to prepare for this event -- such as obtaining information about their pension accounts, their health care coverage and so on.

It is worth noting that among all but the youngest age group, 40-44, women are more likely than men to plan voluntary retirement before 70. For example, among those 61 and older, 46 percent of the men expect to teach until age 70, compared to only 31 percent of the women.

Predictors of Plans for Mandatory Retirement

To identify the variables that best predict the intention to teach until age 70, we carried out an "automatic interaction detector" (AID) analysis, a multivariate procedure analogous to multiple regression, but more powerful in that it takes into account interaction among the predictor variables. The AID computer program searches for the dichotomization that explains more variance in the criterion variable (expectation of retirement at age 70) than any other. The end product of this AID analysis resembles a tree, in which the most powerful variables lead to smaller branches. We fed into this analysis 28 variables that we considered good predictor candidates -- ranging from demographic and institutional characteristics (e.g., sex, type of school) to current circumstances (e.g., enjoyment of teaching, need for salary) to expectations (e.g., anticipated level of retirement income, various hopes and fears about retirement).

Among senior faculty 61 and older, the most powerful predictor of plans for mandatory retirement was the expectation of an inadequate income during the first year or so of retirement. Eighty percent of those who expect their immediate

retirement income to be inadequate plan to stay until they are 70, compared to only 40 percent of those who expect their income to be adequate.

And among those who fear the worst about their immediate retirement income, the influence of family provides further differentiation. Ninety-three percent of those who anticipate an inadequate retirement income and who were influenced by their families to continue working, plan to teach until age 70, compared to 71 percent of those who were also worried about retirement income but were not influenced by their families to stay on.

Other factors influence those who expect to have sufficient retirement income. Among these persons, it is the need for facilities and/or collaborators that figures in the decision to take mandatory retirement. Fifty-six percent of those who expected to have enough money but who needed facilities and/or collaborators expected to stay until 70, compared to only 28 percent of those who were neither worried about money nor about the accessibility of facilities.

Incentives for Voluntary Retirement

When we asked faculty how their retirement plans coincided with what they ideally would like to do, 33 percent of the oldest faculty (61 and older) reported that they would like to retire earlier than they expected to. Thus, one-third of these senior faculty presumably would be receptive to incentives for early complete retirement or phased retirement. To estimate savings in teaching years associated with various incentives, we presented faculty with five hypothetical plans -- two for phased retirement and three for early complete retirement.

Faculty were to assume that the two plans for phased retirement would be available at age 60.

Both plans recognized the importance of key-fringe benefits -- both provided that (1) faculty would receive their current medical benefits through phased retirement, and (2) after full retirement they would receive whatever was currently available to fully retired faculty at their institution. The schools' contributions to their pension funds would continue at the current percentage level until full retirement was taken. The two plans differed in only one way -- the level of financial remuneration. In Plan 1 faculty were offered 60 percent of their full-time salary for half-time work. In Plan 2, they were offered 70 percent of their full-time salary for half-time work.

Faculty were asked at what age they would take phased retirement under each of the two plans and at what age they would completely retire. From this information we calculated for each faculty member the number of teaching years remaining given a certain incentive plan, and we compared this figure with the number of years the faculty member expected to teach before he or she was presented with the incentive plan. The difference between these two figures is the "savings" from expected teaching years provided by the incentive plan. We prorated the number of teaching years during phased retirement according to the proportion of full-time salary received. Thus, under the first plan, which offered 60 percent salary for half-time work, each year of phased retirement was equal to 0.6 teaching years.

Not surprisingly, the plan which offered 70 percent pay was more popular than the one which offered 60 percent pay -- "more popular" in the sense that more faculty said they would change their previous plans in order to take phased retirement under these conditions. However, because we prorated the phased teaching years according to the proportion of salary received, the actual years saved by the two plans was virtu-

ally the same. For instance, among senior faculty 61 and older, each plan provided an average savings of one-half a teaching year (0.5). About two out of five senior faculty would accept the plan that offered 70 percent pay, and about one out of three would take the plan that offered 60 percent pay.

After considering the plans for phased retirement, faculty were presented with three hypothetical plans for early full retirement. They were to assume these plans would be available when they reached age 62. Again, key fringe benefits were provided by the plans. All three continued current medical benefits throughout retirement. In addition, retired faculty would be offered "all usual university courtesies". These plans guaranteed retired faculty specific income levels: that is, if the faculty member's combined income from social security and teaching retirement fund did not equal a specified proportion of the gross salary during the final year of teaching, the school would make up the difference. The plans differed in the level of these guarantees and in their provision of cost-of-living adjustments.

- The first plan provided retirement payments equal to 40 percent of gross salary. No cost-of-living adjustments.

- The second plan offered payments equal to 40 percent of gross salary with annual cost-of-living adjustments until the retired faculty member reached the "normal" retirement age at his or her school.

- The third plan offered retirement payments equal to 60 percent of gross salary. No cost-of-living adjustments.

Again, we asked faculty at what age they would retire completely, given each of these plans, and compared this with the age they expected to retire

without any incentives. We could not, of course, prorate the savings by the proportion of guaranteed salary since the actual cost to the schools would depend on the salary level of the faculty who accepted these plans, and on their longevity.

The most popular plan for complete retirement was the one that offered 60 percent of gross pay and no indexation. Keep in mind that the only plan that offered any indexation did so on a very limited basis — that is, only until the faculty member reached the "normal" retirement age, which at some schools would be as early as age 65 or so. This plan was much less appealing to faculty since it offered only a guarantee of 40 percent of final gross pay.

Among the faculty 61 and older, about one-third indicated they would retire earlier than they expected to if offered guaranteed retirement payments equal to 60 percent of final gross pay. The plan yielded an average savings per faculty member of just under one year (0.9 years). The plan that provided limited indexation and 40 percent gross pay was less appealing — about one-fifth of the oldest faculty would retire earlier under this plan, which yielded an average savings of less than half a teaching year (0.4 years). The plan offering 60 percent pay thus appealed to about the same number of faculty as those reporting they would like to retire earlier than they expected to. The plan which offered 40 percent pay and no indexation was least popular — only about 15 percent of the oldest faculty would retire earlier offered such a plan — the average savings was 0.4 years.

All the plans were more appealing to younger faculty than to those over 60 — for example, among those 50-54, 49 percent reported they would retire earlier given the 60 percent pay plan, compared to about one-third of those over 60.

Also, the 50-54 year-olds provided greater savings -- 1.4 years versus 0.9 years for the oldest faculty.

Effect of Future Inflation on Retirement Intention

It is well to remember that when the study was done (fall of 1979), inflation was at an annual rate of about 10-11 percent and still climbing; that winter it reached an annual rate of about 18 percent. When asked how inflation would affect their retirement plans, 43 percent of the oldest faculty reported that if inflation continued between 9-11 percent, they would change their current plans and work longer. An additional 20 percent would work longer if inflation rose as high as 15-17 percent.

To summarize very briefly, we found that in late 1979 the majority of faculty expected to retire voluntarily before 70 and many indicated they would change their plans and retire even earlier if offered incentives to do so. Whether or not they follow through on these intentions seems to depend largely on the rate of inflation in the coming years. If the economy returns to an extensive period of very high inflation -- say between 15 and 17 percent -- most faculty indicated they would change their plans and postpone their retirement.

Financial Planning for Retirement

George Barbee

Mr. Barbee, a graduate of Brown, is the Executive Director and Founder of The Consumer Financial Institute located in Newton, Massachusetts. The Institute is the largest independent provider of personal financial planning and pre-retirement programs in the United States.

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My thanks to the COFHE group for inviting me here today. I rather like my role which is to suggest to you that there are "transferable learnings" from our work with private sector companies that are applicable to the issues surrounding college faculty retirement. Additionally, we provide self-help financial education to thousands of consumers nationally which may also provide another perspective from the outside.

I'd like to begin by sharing some brief observations I had after reading over the COFHE studies. Then I will cover: the faculty as consumers; the need for a triangle of partnership between the individual faculty member, the educational institution, and the government; strategies for the individual; and strategies for the institution.

Observations on the COFHE Faculty Retirement Study

In reading the COFHE studies, I was struck by the conclusion that personal finances were of primary interest to academic faculty at all age levels, even though historically they have had other priorities. Faculty are now facing a

confrontation between inflation and retirement.

It seems that it is not a question as to "whether" some action will be taken by institutions, but "what" will be done and "when" and "how" much it will cost. There is a great need for practical solutions at this point.

I was also struck by the low level of financial knowledge reflected in the COFHE studies. There were relatively few faculty with specific plans for themselves after retirement. Many others had little specific knowledge of the retirement plans of their institutions.

I couldn't help but ask myself if these situations weren't aggravated by the insulation of faculty from the private sector. Perhaps the compensation philosophy at these institutions -- which may provide such "perks" as subsidized housing, children's tuition assistance, and so on, -- is tending to foster this insulation.

The Faculty As Consumers

Now, I'd like to move on to a simple, but sometimes overlooked observation. The faculty member is also a consumer. As such he or she is subjected to the same factors affecting consumers as a whole regardless of the academic environment.

From our perspective at the Consumer Financial Institute where we have worked with tens of thousands of consumers, many of whom are educators, the following trends are affecting faculty consumers: 1) record high inflation, 2) dependence on two income families, 3) personal tax bracket creep, 4) general aging of the population, 5) higher personal stress related to family finances, and 6) pressures on traditional government and private sector funding of retirement -- such as the need for indexing due to inflation and the

increasing numbers of people drawing pensions.

These pressures in the economy and everyday life of each consumer in the 40 plus age range are happening to everyone, not just tenured college professors. Therefore, there is no cause for paranoia! In this sense, the tenured faculty retirement issue is a microcosm of a larger social and economic issue facing the country.

The Triangle of Partnership

I would now like to discuss the triangle of partnership. The triangle consists of, the individual faculty member, the educational institution - both the college or university and TIAA/CREF, and the government in the form of social security.

At a time of financial priority setting and tight budgets, the tendency is for everyone to point the finger at the other two areas and pass blame and responsibility. Instead, our experience indicates that if a true partnership atmosphere of give and take is established, the solutions can be creative and positive.

Of the three points on the triangle, however, we would have to recognize that the individual has perhaps the greatest distance to come in understanding his or her role in their own retirement and financial planning. Realistically government and college "pockets" are only so deep!

Strategies for Individual Faculty

It is important to look at strategies for the individual. While the population as a whole is plagued by the problems of inflation and personal finances, those approaching retirement have an additional problem. They must deal with the emotional problems brought on simply by the word

"retirement." It is a negatively charged word, often meaning "the end" when the need is for "continuing" or "change." Most individuals are fearful as they approach retirement because our culture has established dreams, myths, and false expectations.

Thus the need for a new word for "retirement." We call it "Stage II". We must realize that retirement today can be a beginning and a change. This can be very positive. If viewed and discussed in this light, we can begin to change the attitude in each community and each individual. So, let's begin to strike the word "retirement" from our vocabulary and talk instead of "change" and "continuation"...Stage II.

There appear to be three parts for an individual's successful launch into Stage II. First I will discuss psychological goal setting and self assessment, then planning time allocation, and finally, personal financial planning.

Strategy A

As far as psychological goal setting and self-assessment, there seem to be 3 categories of people facing Stage II. Let's identify them as "Dans", "Jeans" and "Roberts."

For "Dan," his job is his hobby, his identity. He knows or cares about little else. He is dedicated. He is not eager to leave his job. Money may or may not be a factor.

"Jean," on the other hand, is looking forward to new adventures. Jean has a high energy level and has put off pursuing alternative interests ...now is the time. She has enjoyed work, but wants to use this time of life to experience other interests, both work- and non-work-related. Jean has been anticipating this as an opportunity for

change and growth.

"Robert" has been sticking it out. He has probably not been a high producer. He is relieved that he can finally leave his work. Robert will probably leave seeking escape from perceived drudgery and peer rejection.

Most faculty, we'd presume, are "Dans" or "Jeans". The "Roberts" will probably have sought the opportunity for escape or have been drummed out by peers. From a personal viewpoint, a "Dan" can become, or secretly may want to become, a "Jean"...Dan just has not spent the time exploring it. The essential opportunity is in opening up alternatives. How can we help Dan divert his resources and strengths to new areas or to related areas... to areas that are likely transfers of his strengths or accomplishments? If we begin early, Dan may see alternatives and become a seeker of new challenges.

An important part of Stage II, then, is good coaching and stimulation of self-analysis, resulting in gradual experimentation into new frontiers of interest.

This coaching can be stimulated by the university or college in a partnership environment. It will be personally stimulating to the "Dans," and by opening up alternatives, the university will benefit from more faculty seeking outside challenges during their second stage. This is a positive philosophy of increasing options and choice...and sources of income. Everyone can win!

Strategy B

The second part of Stage II is planning time allocation. The faculty member should analyze the way time is spent now (e.g., 3 hours in class, 2 hours on research, and 4 hours with peers and

students). Then he or she should project how ideally the day would be spent in Stage II. This shift in activity level may occur in stages. There are a great many useful exercises in aiding thinking in this area, but we will pass on further details at this point.

Strategy C

The third part is personal financial planning; perhaps the most important. The faculty member should be encouraged to keep the financial house in order. It is best to start <u>early</u>, while he or she is in the late thirties or early forties. He or she should organize all aspects of personal finances - investment, savings, retirement, insurance, taxes, and estate planning, then set objectives. These objectives should be very specific - not "I want to retire comfortably and travel" but "we will need 70% of our current income."

The individual then must project financial needs given inflation and review these needs in light of his or her own resources. Then he or she must plan strategies to accomplish those goals, and implement them early.

These are steps we've learned from experience are necessary for successful financial planning. Most of us don't take the time to exercise these disciplines early enough in life. This is perhaps one of the most important opportunities for partnership coaching between the faculty and the administration.

<u>Strategies For Institutions</u>

Here we should consider strategies for the institution. Should the institutions begin sponsoring financial planning and Stage II type programs? Waiting until 64 to plan for retirement

at 65 can be a disaster. The hundreds of organizations we've worked with say it is important to start early to develop a long range financial plan, and to experiment to learn about yourself and your interests.

Sponsoring such programs and starting early is just now becoming accepted and popular in organizations we've worked and talked with. It's good for the individual and the parent organization. It opens up options and choices while there is time for experimentation.

Services Available

What types of services are available for financial planning and retirement planning? There are basically two kinds: financial services companies and independents. The financial services organizations include banks, stockbrokers, insurance salesmen, and financial planners. They will provide seminars or personal counseling. While generally inexpensive, and useful from the point of view of ready implementation, these services are often perceived as sales fronts to sell their products. They tend to specialize in their major area of expertise and often do not take an overview of all areas of personal finance. Still, many individuals are good and professional. It simply takes careful examination and experience to recognize them.

There are two kinds of independents — financial education and planning groups, and pre-retirement planning organizations. These organizations will provide seminars and counseling. Some have programs that can be done on an independent, at-home basis. Some use a personalized written analysis to help plan one's finances. Some will use their own staff to provide counseling. Others will help "train the trainer" so as to use your resources.

While individual fees for such programs range from under $100 to $6,000 where in-depth personal counseling is desired, they are objective, professional, and generally should be expected to take an overview of the total financial or retirement picture.

A few pioneering organizations combine the rigors of personal financial education with help in other aspects of anticipating retirement. "Retirement Counseling" per se has historically been done by "social" and government agencies, and a few sponsors in the labor movement. Most are weak in the financial area. "Financial Planning" has historically been done piecemeal by specialists, many of whom have an "axe to grind" because they're selling a product or service (e.g., insurance, stocks, trusts, etc.) There is a need for combining these two areas, and especially tailoring it to the highly educated, sophisticated faculty audience that one finds at colleges and universities.

There are several noteworthy successes and experiments in the private sector. Watching developments in the private sector may provide "lead indicators" and generate ideas for colleges and universities. There are many examples: "No policy" of mandatory retirement; "big brother" programs in which a retired employee is assigned to a rising star; consulting organizations set up by the company made up of retired employees; 20% part-time work - so that the employee can still qualify for benefits; financial planning for all levels and ages of employees starting at age 30; early retirement incentive programs; "outplacement" programs to help poor performers find alternatives.

Realistic Program Goals

What are realistic goals of financial and

stage II planning? These programs can sensitize each individual to his or her role in the planning process (not just government contributions, university pension program, etc.); raise level of individual expertise in managing money and planning retirement; start the thinking process early about personal transfer for "income flexibility"; and encourage each person to plan a personal investment strategy now, while there is time to capitalize on interest compounding.

Criteria Checklist

I have developed a checklist which can be used to evaluate financial planning programs. Such a service should be objective, unbiased, confidential, personalized, reasonably priced, and presented with the appropriate level of sophistication. Also worth considering are whether the provider gives an overview or a specialized perspective, how much administrative time is required, and whether the program is designed for home study or group presentation. These days, a worthwhile financial program must address problems of inflation, and be able to tailor the presentation for all ages from the 30s through the 60s.

Conclusions

In conclusion, let's remember to strike the word "retirement" from our vocabulary. It will limit the people who will attend programs and it has a negative connotation. Begin early... now. Personal financial planning is a desired service for faculty 40 and over and it's "ok" to attend such sessions. It lets faculty formulate plans while there's sufficient lead time to experiment with choices.

Training in personal finances is necessary for raising consciousness of the individual. It is important to stimulate this leg of the triangle so

that the individual will not be solely reliant on the institution and government. Consider using one-time, early retirement incentives to relieve the pressure among older faculty. This could be very inexpensive relative to other costs if faculty stays on and can be attractive to individuals too. Consider establishing a network of part-time employment opportunities among Consortium members and other universities. The private sector can serve as a lead indicator. Look for examples and successes in private industry; they have a 2 to 4 year lead in dealing with the changes in the mandatory retirement situation.

These have been some of my reflections based on the experience we have had at the Consumer Financial Institute working with tens of thousands of individuals across the country, as well as several hundred organizations in the private sector. I think these organizations can be lead indicators. Many of their experiences can be translated to help provide solutions to your needs.

And a last thought... the problems of changing retirement laws, inflation, stifled succession in organizations, etc. are not peculiar to colleges and universities. There are a variety of promising solutions currently available, and new ones are evolving from a "partnership" atmosphere created by the 3 points on the triange: individual, organization and government. As the leading universities in the country, there is an opportunity for each of you to provide a leadership role in this partnership.

Closing Remarks by Dean Lemonick

Colin and Kay have forged a magnificent instrument, and I for one think their work is not yet over. I believe that they are willing to have members of this conference help them set an agenda for the future. I think we need that effort and you are all invited to write directly to them about your own feelings.

Let me end with a short story I once heard related by Martin Trow, Director of the Center for Studies in Higher Education at Berkeley, which seems to be a particularly appropriate way to end this conference.

> At about the turn of the century, the story is told, a fisherman on the Isle of Aran, an island which stands in the Atlantic to the west of Ireland, was reflecting on his life and work, and he did so in these words: "A man who is not afraid of the sea will soon be drowned, for he will be going out on days when he should not. But we do be afraid of the sea, and we do only be drowned now and again."

We are, all of us afloat on the stormy and uncertain sea that is the last quarter of the 20th Century; we have no choice to go out on it. But we are well advised to fear it and study its ways. If we are both wise and lucky, we may like the fisherman of Aran, only be drowned "now and again".