APPROVED
SEP 2 - 1974

Ceremony & Statement 9/2 - Rose Garden

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

AUG 27 1974

MEMORANDUM FOR THE PRESIDENT

To Archives 9/3

Subject: Enrolled Bill H.R. 2 - Employee Retirement Income Security Act of 1974
Sponsors - Rep. Dent (D) Pennsylvania and Rep. Perkins (D) Kentucky

Last Day for Action

We believe that this bill should be acted on at the earliest possible time to minimize the possible cost impact of the termination insurance provisions of the bill, which are effective in part back to July 1, 1974.

Purpose

Establishes standards governing private pension plans, including reporting, disclosure, participation, vesting, funding, and fiduciary responsibilities, and authorizes a Pension Benefit Guaranty Corporation. (The administrative expense costs and the revenue loss from the tax provisions are summarized in a separate section near the end of this memorandum.)

Agency Recommendations

Office of Management and Budget	Approval
Department of Labor	Approval (Signing statement attached)
Department of the Treasury	Approval
Civil Service Commission	Approval
Department of Health, Education, and Welfare	Approval
Department of Housing and Urban Development	No objection
Department of Commerce	No objection
Department of Justice	Defers to other agencies

Discussion

H.R. 2 is a comprehensive private pension reform bill, which represents the Congressional response to legislative initiatives of the Executive branch in the 92nd and 93rd Congresses. It is the result of the combined efforts of the Senate Labor and Finance Committees, and the Ways and Means and Labor Committees in the House.

Currently, there is no comprehensive body of Federal law on private pension plans. The Welfare and Pension Plans Disclosure Act gives the Secretary of Labor powers to require certain reports by pension managers and to investigate suspected abuses, and also authorizes criminal penalties for certain abuses. However, it does not place substantive requirements on pension plans nor does it provide a legal remedy for workers whose pension funds have been squandered by irresponsible trustees.

In addition to Labor's limited authority, Treasury has accorded since 1942 special tax benefits to qualified retirement plans established by employers for the benefit of employees and their beneficiaries. The availability of these special tax benefits is conditioned upon the plans' meeting certain statutory requirements.

The private pension system has played an increasingly important role in providing retirement income to Americans. Benefits paid out by the private pension system increased from $1.7 billion in 1960 to almost $7.4 billion in 1970. During this same period, private pension coverage increased from 21.2 million employees (36 percent of the private work force) to approximately 30 million workers (48 percent of the private work force). Plan assets increased from $52 billion to $138 billion and are increasing at a rate of $12-$15 billion a year. It will not be long before such assets become the Nation's largest source of capital in the economy, and one which is largely unregulated.

This growth in pension plans has brought with it problems. Many workers have not benefited from these pension plans because they had no right to a pension when they left before retirement age or because plans terminated without sufficient funds to pay the expected pensions. In addition, some pension funds have been invested primarily for the benefit of the companies or plan administrators, not for the workers. The need for remedial legislation has been widely recognized for some time.

While not requiring the establishment of pension plans, H.R. 2 would set up major new standards to govern the private pension area, with the goal of increasing the assurance that a worker will receive upon retirement the benefits he expects from a private pension plan. The bill would

-- extend the coverage of the existing private system to more workers by requiring earlier participation in plans

-- strengthen the pension obligations of employers by requiring earlier vesting and more adequate funding

-- require that pension plan assets be managed prudently and in the interests of plan participants

-- insure that reasonable pension obligations will be met in the event that an employer sustains unexpected economic hardship or where there is a sharp decline in a plan's assets

-- assure that plan participants are fully informed of their rights and benefits

The major provisions of the bill are summarized below.

Participation and vesting

H.R. 2 would establish strict rules for participation and vesting in pension plans. In general, these new rules would apply to tax qualified pensions, profit sharing and stock bonus plans, and to employer or employee organization plans established in or affecting interstate commerce.

Under H.R. 2, a pension plan would, in general, be required to allow an employee, who is at least 25 years old and has had at least one year of service, to participate. However, if the plan provides full and immediate vesting to all participants, the one year of service could be extended to three. Plans would be permitted to exclude from participation new employees who are within 5 years of normal retirement age.

This maximum age exclusion is designed to prevent discrimination in the employment of older workers, for whom the cost of benefits in defined benefit plans (ones which pay specific benefits) is high.

Vesting provides a non-forfeitable right to workers to get benefits at retirement age, whether or not they remain employed by the plans' sponsors until they are eligible for retirement. H.R. 2 would establish new Federal standards for vesting in covered plans in addition to the requirement of present law that an employee be 100 percent vested in his accrued benefits upon reaching normal retirement age.

Specifically, plans would be required to provide vesting which meets one of three alternative minimum standards:

(1) Under the 5 to 15-year graded standard, partial vesting would result immediately after 5 years, and rise gradually to full 100 percent vesting after 15 years.

(2) The 10-year/100 percent standard would provide full and immediate vesting after 10 years of covered service. In its recommendations to the conference committee, the Administration opposed the use of this standard on the grounds that it would maximize the incentive for employers to terminate employees approaching 10 years of credited service, and it would perpetuate the presently uneven enforcement practices of the Internal Revenue Service.

(3) The "rule of 45" vesting standard is based upon the Administration-proposed "rule of 50." The rule would provide vesting based upon both an employee's age and credited service in such a way as to provide older employees with more rapid vesting than their younger counterparts.

The enrolled bill would, for the first time, establish standards governing the rate at which workers earn pension benefits. Plans would be required to satisfy one of three benefit accrual tests designed to limit the extent to which vesting standards could be circumvented by providing very low accrual rates in the early years of participation and high rates in later years ("backloading"). While the Administration had previously recommended even stiffer limits, the bill would generally accomplish the Administration's objectives without creating unnecessarily harsh transitional problems for a significant number of existing plans.

In general, the new rules for participation and vesting would apply to plan years beginning after the date of enactment. However, for plans in existence on January 1, 1974, the new rules would apply to plan years beginning after December 31, 1975.

Funding

In practice, present law requires that employers annually contribute to a "defined benefit" pension plan the normal costs of the plan plus interest on past service liabilities. H.R. 2 would strengthen existing law by, in general, requiring that--in addition to normal costs (the costs attributable to current service)--the annual contributions by employers must include amortization of past service liabilities and the pattern of actuarial gains and losses. Specifically, it would require that initial past service liabilities and past service liabilities arising from plan amendments be amortized over periods of no more than 30 years or 40 years depending on type of plan, and that actuarial gains and losses be amortized over no more than 15 years or 20 years. However, unfunded past service liabilities on the effective date of the new funding rules may be amortized over no more than 40 years for plans in existence on the date of enactment to lessen the immediate cost impact.

The Administration supported rapid funding of pension obligations. While the funding standards of the enrolled bill are somewhat less stringent than those advocated by the Administration, the differences will not be significant in the long run.

Termination insurance

Under present law, when a "defined benefit" plan terminates with insufficient assets to cover vested benefits, there is essentially no recourse available to participants for lost benefits. This unfortunate situation results even where the asset insufficiency is a consequence of the employer's failure to adequately fund promised benefits.

The enrolled bill would create a Government corporation, the Pension Benefit Guaranty Corporation, which would insure the vested benefits rights of participants in tax-qualified, defined benefit plans. Although located "within" the Department of Labor, the new corporation would be under the policy guidance of a three-person board of directors comprised of the Secretaries of Labor, Commerce, and Treasury, with the Secretary of Labor to be chairman.

Vested benefits in defined benefit plans would be insured, up to a limit of 100 percent of high-5 consecutive year wages or $750 per month, whichever is less. The $750 limit would be automatically adjusted to reflect changes in social security contributions and benefit base.

The basic program would be required to be self-financed through mandatory premiums levied on covered plans. Initially, these annual premiums would be $1 per participant in single-employer plans and fifty cents per participant in multiemployer plans. With the consent of Congress by concurrent resolution, future premiums could be based upon factors which better reflect the risks involved. The limits on premium rates in the bill may prevent the collection of sufficient premiums to cover the corporation's losses and expenses. The concurrent resolution feature is unfortunate since it raises the constitutional issue of separation of powers, but it can be dealt with appropriately at a later time; one option would be to change the premium rates by law.

In general, where plans are terminating voluntarily, the corporation would pay the insured benefits which could not be covered by plan assets. Amounts paid by the corporation become liabilities of the employer up to 30 percent of his net worth. This portion of the unfunded vested benefits becomes a binding obligation of the employer.

The corporation would also be authorized to institute involuntary terminations of covered plans where such action is deemed to be in the best interests of either plan participants or the corporation.

The bill would also require the corporation to make available contingent liability insurance coverage which would relieve employers from liability arising out of a plan termination after paying an additional premium for five years. However, the corporation is instructed to attempt with private insurers to devise within 36 months after enactment a system for contingent liability coverage involving private insurer participation.

The contingent liability insurance program is intended to eliminate the problems which employers might face with respect to access to credit and capital markets as a result of employer liability. At the same time, however, employer liability is regarded as a key deterrent to abuses by employers of the basic insurance program. For these reasons, the Administration recommended to the conference committee that the corporation be authorized rather than mandated to offer contingent liability coverage. In this way, the difficult issues involved could be given additional study.

The workability of this program is doubtful. The risk assumed is the future profitability of a firm, which will be extremely difficult to assess. If premiums are set high enough to cover risks, sound firms might not buy this insurance; and premiums for others would have to be raised higher. If premiums are set too low, the Government would probably end up subsidizing unwise pension promises.

The corporation is also authorized to develop insurance programs covering benefits related to pensions other than the benefits covered under the basic insurance programs.

Benefits under the basic insurance program would be payable in the case of single employer plan terminations occurring after June 30, 1974; for multiemployer plans, December 31, 1977.

In addition to the extremely difficult implementation problems resulting from these early effective dates, the pre-enactment coverage of single employer plan terminations raises special difficulties. Specifically, for single employer plans terminating between July 1, 1974 and the date of enactment, there would be no employer liability for amounts paid out by the corporation. As a consequence, there would be a significant incentive for employers to terminate their plans during the pre-enactment coverage period. A surge of such induced terminations could create immediate financial difficulties for the corporation as well as aggravate the already difficult operational problems of implementation.

Fiduciary responsibilities

To protect against mismanagement of pension plan funds, H.R. 2 would impose certain fiduciary standards. The new standards would apply generally to all employee benefit plans except Government, church, and workmen's compensation plans, or unfunded plans primarily devoted to providing deferred compensation for a select group of management or highly compensated employees.

To ensure the integrity of plan management, H.R. 2 would impose three strict rules on what a person, acting in a fiduciary capacity, may and may not do with plan assets:

(1) "Prudent Man" rule--The bill would require that each fiduciary of a plan act with the care, skill, prudence, and diligence that a prudent man would use in similar circumstances. Also, the fiduciary must act solely in the interest of the plan's participants and beneficiaries.

(2) Diversification of investments--H.R. 2 would require fiduciaries to diversify plan assets to minimize the risk of large losses unless, under the circumstances, it is clearly prudent not to do so.

(3) Prohibited transactions--The bill would prohibit fiduciaries and parties-in-interest from engaging in a number of specific transactions; for example, the direct or indirect sale, exchange, or leasing of any property between the plan and a party-in-interest would be prohibited. However, in order to avoid unnecessary disruptions, the Secretaries of Labor and Treasury are given authority to grant administrative exemptions or variances.

The Department of Labor will have the responsibility for enforcing fiduciary standards and provisions relating to prohibited transactions by fiduciaries, and Treasury the authority to assess an excise tax on parties-in-interest who violate the new prohibited transaction rules.

Reporting and disclosure

Reporting and disclosure requirements enable plan participants and beneficiaries to protect their interests by keeping them informed of plan management and of their rights and benefits.

H.R. 2 strengthens the reporting and disclosure requirements of existing law by requiring detailed reporting of the financial transactions and status of a plan. These requirements, to be administered by the Secretary of Labor, are applied to all pension and welfare plans established or maintained by an employer or employee organization engaged in, or affecting, interstate commerce. Government plans, certain church plans, workmen's compensation, and unemployment compensation plans would be excluded.

Plans would be required to file an annual report with the Secretary of Labor which would be available for public inspection.

H.R. 2 provides that each administrator of a plan is to furnish to each participant and to each beneficiary a summary plan description written in a manner calculated to be understood by a layman.

The reporting and disclosure provisions generally are to take effect on January 1, 1975.

Portability and non-covered workers

Portability allows workers to take their vested pensions with them as they move from one job to another. Earlier versions of this bill included provisions for a central clearinghouse or Government agency to perform this function.

H.R. 2 would provide a form of portability, advocated by the Administration, by allowing workers to establish individual retirement accounts, into which they can transfer, on a tax-free, roll-over basis, the funds they receive on leaving a job before retirement. Moreover, if the employee moves to a new job he could, with his new employer's consent, transfer funds from his individual retirement account to a qualified plan, under certain conditions.

In addition, under H.R. 2, workers not covered by private or government pension plans would be permitted to contribute to an individual retirement account, on a tax-deductible basis, up to 15 percent of their compensation, but not to exceed $1,500.

Amounts in individual retirement accounts can not be drawn down without penalty before age 59-1/2--except in case of death or disability--and payment of benefits from the account would have to begin by age 70-1/2.

The tax-free roll-over of assets between qualified plans applies to transfers after the date of enactment. The deduction for retirement savings is to be available for taxable years beginning after December 31, 1974.

Administrative provisions and special studies

Jurisdiction under H.R. 2 would be divided between the Departments of Treasury (for tax aspects) and Labor. However, confusion and duplication would be minimized by provisions assigning specific responsibilities for each task, requiring consultation in the development of regulations, and authorizing the development of joint reporting forms.

The bill authorizes the establishment of a Joint Pension Task Force comprised of the staffs of the Committee on Ways and Means and the Committee on Education and Labor of the House, the Joint Committee on Internal Revenue Taxation, and the Committee on Finance and the Committee on Labor and Public Welfare of the Senate. The Joint Task Force is authorized to undertake four studies within 24 months after the date of enactment:

-- a review of the three vesting alternatives in the bill to determine the extent of discrimination, if any, among employees in various age groups resulting from the application of these provisions

-- the means of providing for portability of pension rights among different pension plans

-- the appropriate treatment under the termination insurance provisions for plans established and maintained by small employers

-- the effects and desirability of the preemption of State law provisions of the bill

An additional Congressional study would be authorized to examine the question of whether Federal, State and local government pension plans should be brought under the provisions of H.R. 2.

The bill requires that actuaries must be enrolled to practice before the Department of Labor and Internal Revenue Service; specifies standards for enrolled actuaries; and authorizes the Secretaries of Labor and Treasury to establish a joint board to enroll actuaries.

Miscellaneous provisions

Certain other provisions are worthy of note:

(1) The enrolled bill would increase the maximum deductible contribution on behalf of self-employed persons to the lesser of 15 percent of earned income or $7,500. Special provisions are included for applying this limitation to benefits under defined benefit plans.

(2) H.R. 2 would impose overall limits on benefits and contributions for individuals under qualified pension, profit-sharing, stock bonus plans, and annuities. The purpose of such limitations is to assure that favored tax treatment is applied only to those situations which do not provide excessive retirement income.

The highest annual benefit which could be paid from a defined benefit plan could not exceed the lesser of (a) $75,000, or (b) 100 percent of the participant's average compensation in his high-three-years of employment. Both of these ceilings would be automatically adjusted to reflect cost-of-living increases.

In the case of a defined contribution plan, the annual additions to an employee's account could not exceed the lesser of $25,000 (with an annual cost-of-living increase provision), or 25 percent of the participant's compensation from the employer.

(3) Under H.R. 2, the provisions governing reporting and disclosure, participation and vesting, and funding responsibility, would generally supersede all relevant State laws. The preemption provision is scheduled to take effect on January 1, 1975, except that preemption with respect to plan termination insurance would take effect on the date of enactment.

(4) Under H.R. 2, plans covered by the vesting requirements would be required annually to provide IRS, for transmittal to the Social Security Administration, the names of individuals who have terminated employment during the year, and who have a deferred vested pension. The Social Security Administration would be required to maintain records of the retirement plans in which individuals have vested benefits, and to provide this information to participants and beneficiaries at their request or on their application for Social Security benefits.

Also, the plan administrator is to furnish each person an individual statement giving him the same information which is reported to the Government, so that the individual may enforce his rights to receive his benefit in the courts.

(5) The bill requires that Labor conduct a 2-year study and then report to Congress on the steps necessary to ensure that professional, scientific and technical personnel employed under Federal procurement, construction or research contracts or grants will be protected against loss of pensions or retirement rights or benefits as a consequence of job transfers or loss of employment resulting from terminations or modifications of Federal contracts, grants, or procurement policies. It also requires Labor, within one year after it submits its report, to develop regulations to the extent possible which will provide the protection referred to above. The bill would require Labor to submit any regulations to the Congress, where they would be subject to disapproval by either House within 120 days of continuous session.

In its views letter on the enrolled bill, Justice indicates that it has consistently opposed one House veto mechanisms as violating Article I, Section 7 of the Constitution. While agreeing with Justice's concern, we note that similar provisions are contained in numerous statutes and that previous Administrations have, on occasion, proposed such provisions.

We also have some question whether H.R. 2 or other existing statutes provide a legal basis for the issuance of the regulations contemplated by the bill.

Budget impact

As a result of the many changes made in H.R. 2 in conference, neither Treasury nor Labor has been able to estimate the full budget impact of the bill. We are considering what interim budget actions should be taken now; e.g. deficiency apportionments or supplemental appropriation requests to provide staff for immediate planning and start-up activities. The other specific requirements could then be determined this fall in the regular budget process, and additional supplementals sent to the Congress in January 1975.

At this time, it appears that the maximum budget impact would be as follows (in millions):

	FY 1975	FY 1976
Outlays		
Administrative Costs:		
Department of the Treasury	$ 15	$ 25
Department of Labor	$ 10	$ 20
Insurance Claims	$ 5	$ 40
Less: Insurance Premiums	-$ 30	-$ 25
Net Outlays	-0-	+$ 60
Revenue Loss	$141	$485

The 1975 budget, based on the Administration's legislative request, included a projected revenue loss of $900 million for that year. Outlays were assumed to have been covered by the allowance for contingencies. Thus the net impact on fiscal year 1975 is substantially lower than that forecast in the 1975 budget.

Agency recommendations

Labor recommends approval and indicates in its views letter that:

> "...support for signing the bill is wholehearted. As can be expected in the case of any legislation which is both comprehensive and very technical, it has some troublesome provisions. With experience, we may find it necessary to propose amendments to facilitate the intended operation of the law. However, the bill also has provisions which this Department and the Administration strongly supported throughout the legislative process."

Treasury also recommends approval and in its views letter notes that H.R. 2 "will provide much needed reform in the retirement area and, in general, will provide greater retirement security for all employees."

The Civil Service Commission finds objectionable the personnel provision of the bill which authorizes 63 supergrade positions for Labor, Treasury and the Pension Benefit Guaranty Corporation. Despite these objections, it recommends approval.

Other agencies either recommend approval or no objection.

Although containing a number of features about which we have reservations--particularly the workability of the termination insurance provisions--H.R. 2, on the whole, establishes standards and requirements which the Administration has been seeking and should effectively deal with many of the defects and abuses in the existing private pension system. Accordingly, we recommend approval.

Labor has informally submitted a draft of a signing statement which has already been transmitted to White House staff. We are working with it on a revision of that draft.

Director

Enclosures

U. S. DEPARTMENT OF LABOR
OFFICE OF THE SECRETARY
WASHINGTON

AUG 23 1974

Mr. Roy L. Ash
Director, Office of
  Management and Budget
Executive Office Building
Washington, D. C. 20503

Dear Mr. Ash:

This is in response to your request of August 15, 1974, for the views of the Department of Labor on enrolled enactment H.R. 2, the "Employee Retirement Income Security Act of 1974" (ERISA).

I urge that the President approve this significant new law.

Millions of American workers have waited a long time for reform of the laws relating to private employee benefit plans. ERISA will accomplish the basic reforms needed for both pension and welfare employee benefit plans. It is the product of extensive consideration by the Congress, involving the labor and tax committees of each House and Joint Committee on Internal Revenue Taxation.

While the bill is comprehensive in dealing with the problems of our private employee benefit plans and complex as to its administration, the Labor Department believes that the cost of administering it is fully justified in view of the great social interest inherent in retirement and welfare plan expectations amounting to many billions of dollars.

My support for signing the bill is wholehearted. As can be expected in the case of any legislation which is both comprehensive and very technical, it has some troublesome provisions. With experience, we may find it necessary to propose amendments to facilitate the intended operation of the law. However, the bill also has provisions which this Department and the Administration strongly supported throughout the legislative process. I am sending a detailed report on the bill in which the most significant provisions -- both desirable and troublesome -- are highlighted.

Sincerely,

Peter J. Brennan

Secretary of Labor

Statement for the President on Signing the Pension Reform Legislation

The Employee Retirement Income Security Act of 1974 is one of the most important social reforms to be enacted in many years. It has been long awaited by millions of American workers and retirees, and it will take us a long way toward the ultimate goal of having a nation in which retirement years are free of economic deprivation and fear.

Our private retirement plans are a relatively young institution which went through a remarkable rate of growth over the past four decades. They grew from coverage of about 5 million workers in 1940 to coverage of about 35 million workers and retirees today. Assets held by plans to pay benefits grew during the same period from about 2-1/2 billion dollars to the neighborhood of 185 billion dollars. This rapid growth of private retirement plans took place largely free of government regulation. For such an accomplishment we owe a tribute to free enterprise and our system of labor-management relations. In a sense, it is because of this great accomplishment -- because of the strengths in our system of private retirement plans -- that we are in a position today to put into law measures that will build an even stronger private retirement system.

Many of the provisions in the reform act are complicated and technically worded. This results largely from the fact that retirement plans are very diverse in design and operation. Nevertheless, the basic reform measures in the legislation are easy to understand. They are to ensure that workers do not have to wait too long a time to earn a legal right to retirement benefits under the plan covering their jobs, that workers will have the information necessary to understand and pursue their rights to benefits, and that the money will be there to pay the benefits when retirement comes. In addition, there are new provisions in the tax law to encourage individuals of modest means not working under an employee retirement plan to set aside tax-deferred dollars for retirement. All in all, I hope that through these measures we will have a private retirement system which is reasonably fair to all workers, which leaves room for further innovation, and which will achieve a reasonable balance of retirement income from among personal savings, private employee retirement benefits, and Social Security benefits.

A moment ago I said that we owe a tribute to free enterprise and our system of labor-management relations. Now I wish to expand that tribute in a general way to all of those in private industry, in private life, and in our government who have worked hard to shape this legislation. Indeed, it reflects a mammoth effort of hard work by many people. But especially there is a tribute due to those American workers and their beneficiaries who wrote as best they could to their representatives and officials in government about their disappointments and frustrations under private pension plans. Without them, we would not have the legislation before us now.

In the sense that so many hard working Americans have waited a long time for this legislation, that so many representatives from business and labor have helped to fashion it, and that the legislation has the overwhelming favor of the Congress, it is we, the people, who enact here today the Employee Retirement Income Security Act of 1974. I am very pleased to be among them.

THE SECRETARY OF THE TREASURY
WASHINGTON

AUG 27 1974

Dear Roy:

This is in response to your request for the Treasury Department's views and recommendation on the enrolled bill H. R. 2, the "Employee Retirement Income Security Act of 1974." Since the enrolled bill is extremely long and complex, no attempt has been made to describe it in detail. Instead, a summary is attached for your reference.

Title I of the enrolled bill includes new minimum standards for participation, vesting and funding of retirement plans. Title I also prescribes new reporting and disclosure requirements and rules governing the conduct of fiduciaries. The provisions of this Title are to be administered and enforced by the Department of Labor.

The same subjects also are covered in Title II. Moreover, Title II contains several additional tax-related amendments to the Internal Revenue Code of 1954, including a provision relating to individual retirement accounts and an increase in the tax deductible contributions which can be made for self-employed individuals and shareholder-employees. The provisions of Title II are to be administered and enforced by the Internal Revenue Service.

Since there are similar provisions in both Titles I and II which will be administered by different Departments, there will be overlapping responsibility in many areas covered by this legislation. Title III of the enrolled bill attempts to solve the problems inherent in dual jurisdiction by establishing procedural guidelines to facilitate the administrative coordination and cooperation that will be necessary.

Title IV establishes the Pension Benefit Guaranty Corporation to provide retirement security for employees through a system of insurance against loss of benefits caused by the premature termination of pension plans of which they are participants.

This bill will produce an estimated revenue loss of $141 million in fiscal year 1975. The long-run effect, estimated at 1974 income levels, is a revenue loss of $650 million per year. Moreover, it is estimated that there will be an increase in administrative expenses incurred by the Internal Revenue Service of $15 million in fiscal year 1975 and $25 million in fiscal year 1976.

In general, the bill adopts in modified form recommendations which the Administration made to the 92d and 93d Congresses. Specifically, our recommendations are reflected in the provisions dealing with participation, vesting, funding, fiduciary responsibility and reporting and disclosure. Also, the Administration's "Individual Retirement

Account" (IRA) concept, and our suggestion to increase the deductible contributions which can be made for self-employed individuals and for shareholder-employees, are in Title II of the bill.

On the other hand, we have strongly opposed the termination insurance provision, dual jurisdiction between the Department of Labor and the Department of the Treasury and the prohibition against "nonqualified," unfunded retirement plans. We have recognized the need for some form of termination insurance, but opposed the adoption of the proposed system. Our opposition was due to the failure to develop a program which adequately limits the abuse potential inherent in termination insurance while accommodating the needs of both employers and employees. One of the problems is the development of an adequate mechanism to prevent the employer from establishing a plan, which he terminates shortly thereafter in order to have the insurance corporation, rather than the employer, fund the benefits. One of the solutions provided by the bill is to hold the employer liable for the insured benefits to the extent of 30 percent of his net worth. Although this provision in the bill may prevent abuse in some situations, this potential liability may have an adverse effect on the ability of some employers to maintain the financial credit rating necessary to continue their business.

Our concern about the termination insurance provision had been temporarily lessened by the delayed effective date in both the Senate and House passed versions of the bill. The effect of such a delay would be to allow employers to terminate their plans if they did not want to assume a liability for which they had not bargained. The final version of the bill, however, provides for employer liability as of the date the President signs the bill into law. Thus, employers who have not terminated their retirement plans by the time the bill is signed by the President will not have time to react to the liability created by this program. While employers may avoid such liability by obtaining contingent liability insurance, which the insurance corporation is required to develop, the nature and scope of such insurance has not yet been determined.

As to jurisdiction between the two Departments involved, the recommendations made by the Administration would have given the Department of Labor the principal role in administering the provisions relating to reporting and disclosure and fiduciary responsibility. The Department of the Treasury would have administered the new minimum standards for participation, vesting and funding. The bill, however, provides for administration of retirement plans by both the Department of Labor and the Department of the Treasury. Although there has been an attempt in the bill to coordinate jurisdiction under Title III, it will require the greatest of efforts to avoid duplication, conflicting requirements, inefficient utilization of the Departments and a heavy burden of compliance by plan administrators and employers. It is inevitable that such efforts probably will not be wholly successful.

Finally, the bill will require all pension plans to be funded. Under present law, unfunded arrangements receive none of the advantageous tax benefits bestowed on funded, "qualified" plans, but employers who are not in a position to fund a plan could still promise some retirement benefits. Under the bill, however, these arrangements will have to be funded, and that requirement will in some cases force their termination. We opposed this prohibition against "nonqualified," unfunded plans.

Notwithstanding these problems, the Department of the Treasury feels that this legislation should be signed. It will provide much needed reform in the retirement area and, in general, will provide greater retirement security for employees. The new minimum standards for participation and vesting are extremely important. Employees with long years of employment will no longer be deprived of anticipated retirement benefits. The new minimum standards for funding will insure the soundness and stability of plans. The bill also will provide an incentive for the one-half of the work-force not currently covered by a public or private retirement plan to set aside funds for their retirement in individual retirement accounts. Furthermore, the bill generally will provide a greater degree of comparability between self-employed individuals and shareholder-employees and common-law employees by, among other things, increasing the deductible contributions for self-employed individuals and shareholder employees. The bill also will provide participants with greater access to information concerning the operation of their pension plans.

For the foregoing reasons, it is our recommendation that the President give his approval to the enrolled bill.

Sincerely yours,

William E. Simon

The Honorable
Roy L. Ash
Director, Office of
Management and Budget
Washington, D. C. 20503

Summary of H.R. 2 As Agreed To By The Conferees

Introduction:

Present law encourages employers to establish retirement plans for their employees by granting favorable tax treatment where plans qualify by meeting standards for nondiscrimination and other rules set forth in the Internal Revenue Code. Such qualified plans must cover a specified percentage of employees or cover employees under a classification found by the Internal Revenue Service not to discriminate in favor of employees who are officers, shareholders, supervisory employees, or highly compensated employees. Similarly, the contributions to such plans or the benefits paid out by them cannot discriminate in favor of such employees.

The favorable tax treatment granted qualified plans is substantial. Employers, within certain limits, are permitted to deduct contributions made to these plans for covered employees whether or not the employees' interest are vested; earnings on the plan's assets are exempt from tax; and covered employees defer payment of tax on employer contributions made on their behalf until they actually receive the benefits, generally after retirement when their income and hence applicable tax rates tend to be lower.

H.R. 2 establishes new standards which plans will have to meet. The following is a summary of the major provisions of H.R. 2.

Participation:

In general, an employee cannot be excluded from a plan on account of age or service if he is at least 25 years old and has had at least one year of service. However, if the plan provides full and immediate vesting for all participants, it may require that the employees attain age 25, with three years of service, in order to participate. Furthermore, a defined benefit plan or a target benefit plan may exclude employees who are within five years of attaining normal retirement age under the plan when they are first employed.

Vesting:

Plans must provide full and immediate vesting in benefits derived from employee contributions. With respect to employer contributions the plan must meet one of three alternative minimum standards:

1. Graded vesting: Twenty-five percent after five years of credited service, increasing five percent per year to 50 percent after 10 years, and thereafter increasing 10 percent per year to 100 percent after 15 years.

2. Full vesting: One hundred percent after 10 years of credited service.

3. Modified Rule of 45: Each employee with five years or more of service would be 50 percent vested when the sum of his age and his years of credited service equaled 45, with 10 percent additional vesting for each year thereafter. Each employee with 10 years of credited service (regardless of his age) must be at least 50 percent vested with 10 percent additional vesting for each year thereafter.

In addition, all plans would have to meet the requirement of present law that an employee must be 100 percent vested in his accrued benefit when he attains a normal or stated retirement age. In the case of a plan other than a defined benefit plan, the accrued benefit is to be the balance in the employee's individual account. In the case of a defined benefit plan, the accrued benefit is to be detetmined under the plan, subject to certain requirements. In general, the accrued benefit is to be determined in terms of the benefit payable at normal retirement age. Each defined benefit plan is to be required to satisfy one of three accrued benefit tests:

1. The three percent test: Under this alternative each participant must accrue, for each year of participation, at least three percent of the benefit which is payable under the plan to a participant who begins participation at the earliest possible entry age and serves continuously until age 65 or normal retirement age under the plan, whichever is earlier.

2. The 133 1/3 percent test: Under this alternative, the plan meets the requirements if the accrual rate for any participant for any later year is not more than 133 1/3 percent of his accrual rate for the current year.

3. Pro rata rule: Under this test, the accrued benefit must not be less than the retirement benefit computed under the plan multiplied by a fraction, the numerator of which is the employee's total years of active participation in the plan, and the denominator of which is the total number of years of active participation he would have had if he continued his employment until normal retirement age.

Funding:

New minimum funding standards are established for plans of employers or unions in or affecting interstate commerce and qualified plans. Generally, the minimum amount that an employer is to contribute annually to a defined benefit pension plan includes the normal cost of the plan plus amortization of past service liabilities and experience losses. Minimum amortization payments required are calculated on a level payment basis, including principal and interest, over stated periods of time and are based on all accrued liabilities. If certain conditions are met, the Internal Revenue Service may waive the requirement of current payment of all or part of a year's contributions of normal costs, and amounts needed to amortize past service liabilities and experience losses.

Plan Termination Insurance:

Private defined benefit pension plans are to be insured against loss of benefits by a corporation within the Department of Labor. The directors of the corporation are the Secretaries of Labor, Treasury and Commerce. The insurance program will be funded through premiums charged covered plans. The initial premium is $1 per participant per year ($0.50 for multiemployer plans). Premiums will be established by the corporation for the third plan year for single employer plans and for multiemployer plans beginning in 1978. The benefits guaranteed are the vested retirement benefits under the plan but not to exceed 100 percent of the employee's wages during his highest paid five consecutive years or $750 per month. This amount is to be adjusted to reflect changes in the social security contribution and benefit base. There are a number of limitations on the benefits guaranteed. The principal limitation is that the guaranteed benefits are to be phased in at the rate of 20 percent per year, so that the benefit is fully covered after it has been in effect for five years. Employers must repay the insurance fund for benefits paid to their employees by the corporation but need not pay more than 30 percent of their net worth. The bill contains a provision which would require the corporation to establish a program for insuring this contingent liability. In order to recover amounts from the employer, the insurance company will have a lien on the employer's property which will have a status equivalent to a general Federal tax lien. Furthermore, a trustee may recover certain payments to a participant in order to satisfy obligations under the plan.

Fiduciary Standards:

Rules are provided to govern the conduct of plan fiduciaries under the labor provisions and also the conduct of disqualified persons with respect to the plan under the tax provisions. The labor law provisions apply rules and remedies similar to those under traditional trust law to govern the conduct of fiduciaries. A federal prudent man standard for investments of pension and welfare plan funds is established and State standards are preempted. The labor provisions also provide rules governing the structure of plan administration including the establishment of a plan, plan contents, establishment of a trust, and liability for breach of co-fiduciary responsibility. The tax law provisions impose an excise tax on disqualified persons who violate the new prohibited transaction rules (this is similar to the approach taken under the present rules against self-dealing in the private foundations area).

Reporting and Disclosure:

New comprehensive reporting and disclosure rules are provided in the labor provisions. These new standards are to be administered by the Department of Labor and are to be applied to all pension and welfare plans engaged in or affecting interstate commerce. Provisions will require an annual report which shall include audited financial statements for both welfare plans and pension plans. Furthermore, the new disclosure requirements provide that each plan participant must be furnished with a plan booklet explaining his rights and obligations.

Individual Retirement Accounts:

Any individual not covered by a private or public retirement plan can establish an individual retirement account (IRA) and contribute up to $1,500 annually. Moreover, the individual retirement account may be established by the employer or by the employee's union. Contributions are tax deductible and earnings are tax-free. The amount in the individual retirement account may be set aside in a special trusteed or custodial account with a bank, savings and loan, or credit union, and includes the investment in an annuity contract, or qualified retirement bonds.

Portability:

If an employer distributes benefits immediately to a terminated employee, the employee may transfer his benefits into an individual retirement account to be held for his retirement. Moreover, if the employee later is employed by another employer maintaining a plan he is permitted to contribute the amount in his individual retirement account into the new employer's retirement plan.

Limits on Contributions and Benefits for Self-Employed and Shareholder-Employees:

The maximum annual deduction to a plan for a self-employed individual or a shareholder-employee is increased from the lesser of 10 percent of earned income or $2,500 to the lesser of 15 percent of earned income or $7,500. Moreover, the bill establishes a table which will permit a self-employed individual or a shareholder-employee to establish a defined benefit plan by converting the contribution limits of 15 percent of earned income or $7,500 into an annual benefit to be provided under the plan.

Limits on Contributions and Benefits:

A tax qualified defined pension plan may not pay an annual pension of more than 100 percent of salary or $75,000 per annum. Defined contribution plans are limited to annual contributions no greater than 25 percent of salary or $25,000. The $75,000 and $25,000 figures are subject to a cost of living adjustment.

Lump Sum Distributions:

The bill provides new rules for lump sum distributions which will make it easier for the Internal Revenue Service to administer and for the taxpayer to compute the taxation of lump sum distributions. Distributions attributable to the pre-1973 taxable portion of a lump sum distribution will be treated as a capital gain. On the other hand, the post-1973 taxable portion of a lump sum distribution will be treated as ordinary income taxed under an averaging device which treats it as if it were received evenly over a 10-year period.

Enforcement:

Enforcement of standards is by the Internal Revenue Service, the Department of Labor, and plan participants. Generally, the Internal Revenue Service enforces the tax qualification and the Labor Department enforces violations of standards which result in denial of pension rights.

Organization:

A new office is established in the Internal Revenue Service entitled Office of Assistant Commissioner of Internal Revenue for Employee Plans and Exempt Organizations. The Office will be created within 90 days after the date of enactment. Funds are provided under the bill to administer the new Office of the Assistant Commissioner.

OPTIONAL FORM NO. 10
MAY 1962 EDITION
GSA GEN. REG. NO. 27

UNITED STATES GOVERNMENT

Memorandum

Department of the Treasury
Washington, D.C.

TO : Ralph Malvik, Legislative Analyst
Office of Management and Budget

DATE: August 27, 1974

FROM : Theodore E. Rhodes, Attorney Adviser
Office of Tax Legislative Counsel

TER

SUBJECT: Points to be Included in President's Signing Statement

Attached is a revised copy of the Treasury's Points to be included in the President's Signing Statement. The principal changes made were in the introduction and the first paragraph of the background material. Would you please forward this to the White House.

Attachment

BACKGROUND POINTS FOR USE IN PREPARING PENSION LEGISLATION SIGNING STATEMENT

Introduction:

The "Employee Retirement Income Security Act of 1974" accomplishes comprehensive reform of the private pension system and significantly strengthens the rights of employees to their retirement benefits. It represents the outgrowth of many years of extensive cooperative effort, both within the Administration and in Congress. I am very pleased to sign this bill.

Background:

On December 8, 1971, and again on April 11, 1973, the Administration sent a pension reform message to Congress in which it called for broad changes in the requirements for qualified plans under the Internal Revenue Code, the establishment of new Federal fiduciary standards for pension and welfare plans, and for significant strengthening of Federal reporting and disclosure requirements.

Many members of Congress, including Representatives Dent and Erlenborn and Senators Williams and Javits introduced bills to protect employees' retirement security. During 1973, both the Senate Labor and Public Welfare Committee and the Senate Finance Committee reported out massive pension reform bills. These committees reached a compromise on their bills and the Senate adopted its version of pension reform on September 19, 1973. During 1973 and 1974 the House Education and Labor Committee and the House Ways and Means Committee also reported out pension reform legislation. Through cooperative efforts on the part of both committees, the House passed a bill on February 28, 1974, which combined the features of both bills. Representatives from four committees (Senate Finance and Senate Labor and Public Welfare Committees; House Education and Labor and House Ways and Means Committees) formed a Committee of Conference and began meetings on May 15, 1974. The conferees, their staffs and representatives of the Administration attended numerous meetings over a three-month period during which a spirit of cooperation and compromise prevailed. The four committees reached an agreement and their conference report was subsequently adopted by both Houses.

Objectives:

One of the most important public policy issues facing the nation today is how to assure that individuals who spend their careers in useful and socially productive work will have adequate income to meet their needs when they retire. This legislation is concerned with improving the fairness and effectiveness of retirement income. In broad outline, the objectives are as follows:

--to increase the number of individuals participating in employer-financed plans by establishing minimum standards for participation;

--to make sure to the greatest extent possible, by establishing minimum standards for vesting and funding, that those who do participate in such plans actually receive benefits and do not lose them as a result of unduly restrictive forfeiture provisions or failure of the pension plan to accumulate sufficient funds to meet its obligations;

--to establish standards to insure that fiduciaries discharge their duties solely in the interest of participants and their beneficiaries and in a manner which will not jeopardize the income or assets of the fund;

--to require complete disclosure of information concerning the operations of the employer's retirement plan;

--to increase the fairness of the tax laws relating to qualified retirement plans by providing greater equality of treatment under plans for different taxpayers, such as raising the limits on deductible contributions for the self-employed and shareholder-employees and by allowing the one-half of the work force not covered by the existing pension system equivalent tax advantages through individual retirement accounts;

--to insure the loss of pension benefits due to plan terminations through a new Pension Benefit Guaranty Corporation; and

--to provide for a form of portability through the transfer of benefits of a terminated participant to an individual retirement account.

Administration Views:

H.R. 2 as passed by the House and Senate adopts in modified form recommendations of the Administration in the areas of participation, vesting, funding, fiduciary standards, reporting, disclosure, individual retirement accounts, and limitations on deductions for self-employed individuals.

In developing this legislation with Congress, the Administration has expressed reservations about some of its features. For example, we have been concerned that the liability created under the termination insurance provisions may have some adverse consequences on employers who maintain insured plans. Furthermore, the decision to provide for overlapping jurisdiction between the Departments of Labor and Treasury will require real effort to avoid duplication, conflicting requirements and a heavy burden of compliance by plan administrators and employers. Moreover, those employers who do not fund their employees' pension plans and who therefore receive none of the advantageous tax benefits, will now be required either to fund their pension plans or terminate them.

However, like any good legislative product, this legislation is the result of compromise and adjustments by all parties. We think this is good legislation, strong legislation, and I am most happy to sign it.

U. S. Treasury Department
Office of Tax Legislative Counsel
August 26, 1974

OPTIONAL FORM NO. 10
MAY 1962 EDITION
GSA GEN. REG. NO. 27

UNITED STATES GOVERNMENT

Memorandum

Department of the Treasury
Washington, D.C.

TO : Ralph Melvik
Legislative Analyst, Office of
Management and Budget

DATE: August 21, 1974

FROM : Ernest S. Christian, Jr.
(Acting) Deputy Assistant Secretary

ESC

SUBJECT: Enrolled Bill Report on H.R. 2, "Employee Retirement Income Security Act of 1974"

Per my conversation with Mr. Rommel, attached is a first draft of a proposed enrolled bill report, an attached summary and some suggested points for a signing statement.

I am reviewing these and we will transmit the final form of these papers tomorrow.

Attachment

THE SECRETARY OF THE TREASURY
WASHINGTON

Dear Mr. Ash:

This is in response to your request for the Treasury Department's views and recommendation on the enrolled bill H. R. 2, the "Employee Retirement Income Security Act of 1974." Since the enrolled bill is extremely long and complex, no attempt will be made to describe it in detail. A summary is attached for your reference.

Title I of the enrolled bill includes new minimum standards for participation, vesting and funding and prescribes new reporting and disclosure requirements and rules governing the conduct of fiduciaries. The provisions of this title are to be administered and enforced by the Labor Department.

The same subjects are also covered in Title II. Moreover, Title II contains several additional tax-related amendments to the Internal Revenue Code of 1954, including a provision relating to individual retirement accounts and an increase~~s~~ the deductible contributions which can be made by self-employed and shareholder-employees. The provisions of Title II are to be administered and enforced by the Internal Revenue Service.

The fact that there are similar provisions in both Titles I and II, which will be administered by separate departments, means that there will be overlapping responsibility in many areas covered by this legislation. Title III of the enrolled bill attempts to solve the problems inherent in dual jurisdiction by establishing procedural guidelines to facilitate administrative coordination and cooperation.

Title IV establishes The Pension Benefit Guaranty Corporation to provide retirement security for employees through a system of insurance against loss of benefits caused by the premature termination of pension plans.

This bill will produce an estimated revenue loss of $141 million in fiscal year 1975. The long run effect, estimated at 1974 income levels, is a revenue loss of $650 million per year. Moreover, it is estimated that there will be an increase in administrative expenses incurred by the Internal Revenue Service of $15 million in fiscal year 1975 and $25 million in fiscal year 1976.

In general, the bill adopts in modified form recommendations which the Administration made to the 92d and 93d Congresses. Specifically, our recommendations are reflected in the provisions dealing with participation, vesting, funding, fiduciary responsibility and reporting and disclosure. Also the Administration's "Individual Retirement

Account" (IRA) concept, and our suggestions to restore tax equality by increasing the deductible contributions which can be made for the self-employed and for shareholder-employees, are in Title II. On the other hand, the Administration has strongly opposed the concept of plan termination insurance, dual Labor-I. R. S. jurisdiction and the prohibition against "nonqualified" retirement plans.

The Administration recognized the need for some form of termination insurance, but opposed the adoption of the proposed system. Our opposition was due to the failure to develop a program which adequately limits the abuse potential inherent in termination insurance while accommodating the needs of both employers and employees. One of the probems ⓛ is developing a mechanism to prevent the employer from establishing a plan, which he terminates shortly thereafter, in order to have the insurance corporation, rather than the employer, fund the benefits. The solution provided by the bill is to hold the employer liable for the insured benefits to the extent of 30% of his net worth. Although the proffered solution may prevent abuse in some situations, this potential liability may have a devastating effect on the ability of some employers to obtain credit and, thereby, force them out of business.

Although the Administration opposed this program, our concern was lessened by the provision for a delayed effective date in both the Senate and House passed versions of the bill. The effect of such a delay would be to allow employers to terminate their plans if they did not want to assume a liability for which they had not bargained. The final version of the bill, however, provides for employer liability as of the date of enactment. Thus, employers who have not already terminated their plans will have no time to react to the liability created by this program other than to cover themselves under a yet undefined contingent liability insurance.

As indicated above, the bill provides for administration of pension plans by both the Department of Labor and the Department of the Treasury. The recommendations made by the Administration would have given the Department of Labor the principal role in administering the provisions relating to reporting and disclosure and fiduciary responsibility. The Treasury would have administered the new minimum standards for participation, vesting and funding. To resolve the jurisidictional dispute between the tax and labor committees in Congress, the conferees decided on overlapping jurisdiction between the Departments of Labor and Treasury. Although there has been an attempt to coordinate jurisdiction under Title III, the inevitable result of such a compromise will be duplication of effort and reporting, conflicting requirements, inefficient utilization of the departments and a heavy burden of compliance by plan administrators and employers.

Finally, this bill will require all pension plans to be funded. Presently, unfunded arrangements receive none of the advantageous tax benefits bestowed on funded tax qualified plans. Employers who are not in a position to fund a plan, however, can still promise some retirement benefits (although the benefit will generally be less than that which could be offered if the funds necessary to provide the benefit could accumulate tax free). Under the bill these arrangements will have to be funded, which often will force their termination.

Notwithstanding these problems, the Department of the Treasury feels that this legislation should be signed. It will provide much needed reform in the retirement area and, in general, will provide greater retirement security for all employees. The new minimum standards for participation and vesting are extremely important. Now employees with long years of employment will no longer be deprived of anticipated retirement benefits. The new minimum standards for funding will insure the soundness and stability of plans. The bill will also provide an incentive for the uncovered one-half of the work-force to set aside funds for retirement security in new individual retirement accounts. Furthermore, the bill will generally provide a greater degree of comparability between the self-employed and shareholder-employees and common-law employees increasing the deductible contributions for the self-employed and shareholder employees. The bill also will provide the worker with greater access to information concerning the operations of his pension plan. Moreover, the "rollover" accounts will provide the employee with a means to make his pension benefits portable from one plan to another plan.

For the foregoing reasons, it is our recommendation that the President give his approval to the enrolled bill.

Sincerely yours,

William E. Simon

The Honorable
Roy L. Ash
Director, Office of
Management and Budget
Washington, D. C. 20503

Enclosure

Summary of H.R. 2 As Agreed To By The Conferees

Introduction:

Present law encourages employers to establish retirement plans for their employees by granting favorable tax treatment where plans qualify by meeting standards for nondiscrimination and other rules set forth in the Internal Revenue Code. Such qualified plans must cover a specified percentage of employees or cover employees under a classification found by the Internal Revenue Service not to discriminate in favor of employees who are officers, shareholders, supervisory employees, or highly compensated employees. Similarly, the contributions to such plans or the benefits paid out by them cannot discriminate in favor of such employees.

The favorable tax treatment granted qualified plans is substantial. Employers, within certain limits, are permitted to deduct contributions made to these plans for covered employees whether or not the employees' interests are vested; earnings on the plan's assets are exempt from tax; and covered employees defer payment of tax on employer contributions made on their behalf until they actually receive the benefits, generally after retirement when their income and hence applicable tax rates tend to be lower.

H.R. 2 establishes new standards which plans will have to meet in order to continue their qualified status and, thereby, receive special tax treatment. The following is a summary of the major provisions of H.R. 2.

Participation:

In general, an employee cannot be excluded from a plan on account of age or service if he is at least 25 years old and has had at least one year of service. However, if the plan provides full and immediate vesting for all participants, it may require that the employees attain age 25, with three years of service, in order to participate. Furthermore, a defined benefit plan or a target benefit plan may exclude employees who are within five years of attaining normal retirement age under the plan when they are first employed.

Vesting:

Plans must provide full and immediate vesting in benefits derived from employee contributions. With respect to employer contributions the plan (except class year plans) must meet one of three alternative minimum standards:

1. Graded Vesting: Twenty-five percent after five years of credited service, increasing five percent per year to 50 percent after 10 years and thereafter, increasing 10 percent per year to 100 percent after 15 years.

2. Full vesting: One hundred percent after 10 years of credited service.

3. Modified Rule of 45: Each employee with five years or more of service would be 50 percent vested when the sum of his age and his years of credited service equaled 45, with 10 percent additional vesting for each year thereafter. Each employer with 10 years of covered service (regardless of his age) must be at least 50 percent vested with 10 percent additional vesting for each year thereafter.

In addition, all plans would have to meet the requirement of present law that an employee must be 100 percent vested in his accrued benefit when he attains a normal or stated retirement age (or actually retires). In the case of a plan, other than a defined benefit plan, the accrued benefit is to be the balance in the employee's individual account. In the case of a defined benefit plan, the accrued benefit is to be determined under the plan, subject to certain requirements. In general, the accrued benefit is to be determined in terms of the benefit payable at normal retirement age. Each defined benefit plan is to be required to satisfy one of three accrued benefit tests:

1. The three percent test: Under this alternative each participant must accrue, for each year of participation, at least three percent of the benefit which is payable under the plan to a participant who begins participation at the earliest possible entry age and serves continuously until age 65 or normal retirement age under the plan, whichever is earlier.

2. The 133 1/3 percent test: Under this alternative, the plan meets the requirements if the accrual rate for any participant for any later year is not more than 133 1/3 percent of his accrual rate for the current year.

3. Pro rata rule: Under this test, the accrued benefit must not be less than the retirement benefit computed under the plan multiplied by a fraction, the numerator of which is the employee's total years of active participation in the plan, and the denominator of which is the total number of years of active participation he would have had if he continued his employment until normal retirement age.

Plan Termination Insurance:

Private defined benefit pension plans are to be insured against loss of benefits by a corporation within the Labor Department. The board of directors of the corporation ~~are~~ will be the Secretaries of Labor, Treasury and Commerce. The insurance program will be funded through premiums charged covered plans. The initial premium is $1 per participant per year ($0.50 for multiemployer plans). Premiums will be established by the corporation for the third plan year for single employer plans and for multiemployer plans beginning in 1978. The benefits guaranteed are the vested retirement benefits under the plan but not to exceed 100 percent of the employee's wages during his highest paid five consecutive years or $750 per month. This amount is to be adjusted to reflect changes in the social security contribution and benefit base. There are a number of limitations on the benefits guaranteed; the principal limitation is that the guaranteed benefits are to be phased in at the rate of 20 percent per year, so that the benefit is fully covered after it has been in effect for five years. Employers must repay the insurance fund for benefits paid to their employees by the corporation but need not pay more than 30 percent of their net worth. The bill contains a provision which would allow the corporation to establish a program for insuring this contingent liability. In order to recover amounts from the employer, the insurance company will have a lien on the employer's property which will have a status equivalent to a general Federal tax lien. Furthermore, a trustee may recover certain payments to a participant in order to satisfy obligations under the plan.

Fiduciary Standards:

Rules are provided to govern the conduct of plan fiduciaries under the labor provisions and also the conduct of disqualified persons with respect to the plan under the tax provisions. The labor law provisions apply rules and remedies similar to those under traditional trust law to govern the conduct of fiduciaries. A federal prudent man standard for investments of pension and welfare plan funds is established and State standards are preempted. The labor provisions also provide rules governing the structure of plan administration including the establishment of a plan, plan contents, establishment of a trust, and liability for breach of co-fiduciary responsibility. The tax law provisions impose an excise tax on disqualified persons who violate the new prohibited transaction rules (this is similar to the approach taken under the present rules against self-dealing in the private foundations area).

Reporting and Disclosure:

New comprehensive reporting and disclosure rules are provided in the labor provisions. These new standards are to be administered by the Department of Labor and are to be applied to all pension and welfare plans engaged in or affecting interstate commerce. Provisions will require an annual report which shall include audited financial statements for both welfare plans and pension plans. Furthermore, the new disclosure requirements provide that each plan participant must be furnished with a plan booklet explaining his rights and obligations.

Individual Retirement Accounts:

Any individual not covered by a private or public retirement plan can establish an individual retirement account (IRA) and contribute up to $1,500 annually. Moreover, the individual retirement account may be established by the employer or by the employee's union. Contributions are tax deductible and earnings are tax-free. The amount in the individual retirement account may be set aside in a special trusteed or custodial account with a bank, savings and loan, or credit union, and includes the investment in an annuity contract, or qualified retirement bonds.

Portability:

If an employer distributes benefits immediately to a terminated employee, the employee may transfer his benefits into an individual retirement account to be held for his retirement. Moreover, if the employee later is employed by another employer maintaining a plan he is permitted to contribute the amount in his individual retirement account into the new employer's retirement plan.

Limits on Contributions and Benefits for Self-Employed and Shareholder Employees:

The maximum annual deduction to a plan for a self-employed individual or a shareholder employee is increased from the lesser of 10 percent of earned income or $2,500 to the lesser of 15 percent of earned income or $7,500. Moreover, the bill establishes a table which will permit a self-employed individual or a shareholder employee to establish a defined benefit plan by converting the contribution limits of 15 percent of earned income or $7,500 into an annual benefit to be provided under the plan.

Limits on Contributions and Benefits:

A tax qualified defined pension plan may not pay an annual pension of more than 100 percent of salary or $75,000 per annum. Defined contribution plans are limited to annual contributions no greater than 25 percent of salary or $25,000. The $75,000 and $25,000 figures are subject to a cost of living adjustment.

Lump Sum Distributions:

The bill provides new rules for lump sum distributions which will make it easier for the Internal Revenue Service to administer and for the taxpayer to compute the taxation of lump sum distributions. Distributions attributable to the pre-1973 taxable portion of a lump sum distribution will be treated as a capital gain similar to the present law. On the other hand, the post-1973 taxable portion of a lump sum distribution will be treated as ordinary income taxed under an averaging device which treats it as if it were received evenly over a 10-year period.

Enforcement:

Enforcement of standards is by the Internal Revenue Service, the Department of Labor, and plan participants. Generally, the Internal Revenue Service enforces the tax qualification and the Labor Department enforces violations of standards which result in denial of pension rights.

Organization:

A new office is established in the Internal Revenue Service entitled Office of Assistant Commissioner of Internal Revenue for Employee Plans and Exempt Organizations. The Office will be created within 90 days after the date of enactment. Funds are provided under the bill to administer the new Office of the Assistant Commissioner.

POINTS TO BE INCLUDED IN PENSION LEGISLATION

SIGNING STATEMENT

Introduction:

The "Employee Retirement Income Security Act of 1974" represents a major step toward the adequate protection of the rights of all employees to their retirement benefits. I am particularly glad to sign this bill at this time because it represents the outgrowth of many years of extensive cooperative effort, both within the Administration and in Congress.

Background:

On December 8, 1971 and again on April 11, 1973, the Administration sent a pension reform message to Congress, in which it called for broad changes in the requirements for qualified plans under the Internal Revenue Code and for passage of a "fiduciary" proposal, previously submitted in March, 1970.

Many members of Congress, including Representatives Dent and Erlenborn and Senators Javits and Williams, introduced bills to protect employees' retirement security. During 1973, both the Senate Labor and Public Welfare Committee and the Senate Finance Committee reported out massive pension reform bills. These committees reached a compromise on their bills and the Senate adopted its version of pension reform on September 19, 1973. During 1973 and 1974 the House Education and Labor Committee and House Ways and Means Committee also reported out pension reform legislation. Again through cooperative efforts on the part of both committees, the House passed a bill on February 28, 1974, which combined the features of both bills. Representatives from four committees (Senate Finance and Senate Labor and Public Welfare Committees; House Education and Labor and Ways and Means Committees) formed a "Committee of Conference" and they began meetings on May 15, 1974. The conferees, their staffs and representatives of the Administration attended numerous meetings over a three month period during which a spirit of cooperation and compromise prevailed. The four committees reached an agreement and their conference report was subsequently adopted by both Houses.

H. R. 2 as passed by the House and Senate adopts in modified form recommendations of the Administration in the areas of participation, vesting, funding, fiduciary standards, reporting, disclosure, individual retirement accounts, and limitations on deductions for the self-employed.

Administration View:

One of the most important public policy issues facing the nation today is how to assure that individuals who spend their careers in useful and socially productive work will have adequate income to meet their needs when they retire. This legislation is concerned with improving the fairness and effectiveness of retirement income. In broad outline, the objectives are as follows. First, to increase the number of individuals participating in employer-financed plans by establishing minimum standards for participation. Second, to make sure to the greatest extent possible, by establishing minimum standards for vesting and funding, that those who do participate in such plans actually receive benefits and do not lose them as a result of unduly restrictive forfeiture provisions or failure of the pension plan to accumulate sufficient funds to meet its obligations. Third, to establish standards to insure that fiduciaries discharge their duties solely in the interest of participants and their beneficiaries and in a manner which will not jeopardize the income or assets of the fund. Fourth, to require complete disclosure of information concerning the operations of the employer's retirement plan. Fifth, to increase the fairness of the tax laws relating to qualified retirement plans by providing greater equality of treatment under plans for different taxpayers, by raising the limits on deductible contributions for the self-employed and shareholder employees and by allowing the one-half of the work force not covered by the existing pension system equivalent tax advantages through individual retirement accounts. Sixth, to prevent the loss of pension benefits due to plan terminations by insuring benefits through the Pension Benefit Guaranty Corporation. Seventh, to provide for a form of portability through the transfer of benefits of a terminated participant to an individual retirement account.

In developing this legislation with Congress, the Administration has expressed reservations about some of its features. For example, we believe the liability created under the termination insurance provisions may have an adverse impact on employers who maintain plans. Furthermore, the decision to provide for overlapping jurisdiction between the Departments of Labor and Treasury will inevitably result in some duplication of effort and reporting, conflicting requirements and a heavy burden of compliance by plan administrators and employers. Moreover, those employers who cannot fund their retirement plans and therefore receive none of the advantageous tax benefits, will be required to fund their plans, which may force their termination. However, like any good legislative product, this legislation is the result of compromises and adjustments by all parties. We think this is good legislation, strong legislation, and I am most happy to sign it.

U. S. Treasury Department
Office of Tax Legislative Counsel
August 21, 1974

UNITED STATES CIVIL SERVICE COMMISSION
WASHINGTON, D.C. 20415

CHAIRMAN

August 21, 1974

Honorable Roy L. Ash
Director
Office of Management and Budget
Washington, D.C. 20503

Attention: Assistant Director for
Legislative Reference

Dear Mr. Ash:

This is in reply to your request for the views and recommendations of the Civil Service Commission on enrolled H.R. 2, a bill "To provide for pension reform."

This legislation is intended to protect workers in private industry against loss of pension rights when they switch jobs, or when their pension fund is inadequately funded or abruptly terminated by the employer. It would extend to all private employers engaged in interstate commerce certain reporting, disclosure, and fiduciary standards which were previously applicable only to private employee pension plans receiving preferred tax treatment under section 401(a) of the Internal Revenue Code of 1954. It also provides new participation, vesting, and funding standards which must be met by pension plans of employers engaged in interstate commerce and those which qualify under section 401(a) of the Internal Revenue Code.

Government plans such as the Civil Service Retirement System are exempted from meeting reporting, disclosure, and fiduciary standards. They are also exempted from the new participation, vesting, and funding requirements. Instead, Government plans would be treated as meeting these new requirements for purposes of preferred tax treatment under section 401(a) of the Internal Revenue Code if such plans met these requirements the day before the date of enactment of this legislation.

This legislation would be administered primarily by the Department of Labor and a new Pension Benefit Guaranty Corporation. The Department of Labor would be responsible for fiduciary and other standards, disclosure requirements, and enforcement. The Pension Guaranty Benefit Corporation would be responsible for a pension plan termination program. The Internal Revenue Service would also have a role: to determine whether pension plans qualify for preferred tax treatment.

Title IV provides for the establishment of the Pension Benefit Guaranty Corporation under the direction of a three member Board of Directors consisting of the Secretaries of Labor, Commerce, and Treasury. The Secretary of Labor would be Chairman of the Board with responsibility for program administration.

Under section 4002(b)(6) the Corporation would be authorized to appoint and fix the compensation of such employees as may be needed. These employees would be subject to the regular appointment procedures under title 5, United States Code. There is some question whether they would also be subject to the General Schedule classification and pay system, since employees of certain kinds of nonappropriated fund activities are excluded by law (section 5103 of title 5, United States Code) from the General Schedule system. It will be the responsibility of the Civil Service Commission, under section 5102(c)(14) of title 5, to determine whether the Pension Benefit Guaranty Corporation comes under the section 5102(c)(14) exclusion. We are not prepared at this time to make a final determination on this question.

Section 4002(c) would amend section 5108 of title 5, United States Code, by authorizing the Corporation to establish without regard to any other provision of this section, one GS-18 position and a total of 10 other positions at GS-16 and GS-17. Similar provisions appear in other sections of the bill: section 507(b) which would authorize a GS-18 and 20 GS-16 and 17 positions in the Department of Labor, and section 1051(b) which would authorize a GS-18 Assistant Commissioner position in the Office of Employee Plans and Exempt Organizations of the Internal Revenue Service and 20 positions at GS-16 and GS-17. We find these provisions objectionable. They are inconsistent with the laws authorizing the Civil Service Commission to establish supergrade positions and make it difficult to maintain grade level alignment within an agency and throughout the Executive Branch.

Subsection (h) of section 4002 would establish a seven-member advisory committee to the Corporation. Members of this advisory committee would be paid the daily equivalent of the rate for GS-18. We consider this rate of pay appropriate.

Section 512 of the enrolled bill would establish an Advisory Council on Employee Welfare and Pension Benefit Plans. The fifteen members of this council would be paid the daily equivalent of the rate for GS-18. We view this rate of pay as appropriate for the members of an advisory body of this nature.

Also of interest to the Commission are the provisions in title IV of H.R. 2 dealing with the portability of pensions. They provide that an employee, who changes employers, may irrevocably transfer to an Individual Retirement Account funds distributed to him from his former employer's pension plan, less the amount contributed by him as an employee contribution. Additional funds could be contributed by the employee to this account on a tax free basis until the employee retires.

Investment in such an account is not presently possible for Federal employees. Under the Civil Service Retirement law, refunds paid to separated employees consist primarily of employee contributions which may not be invested in an Individual Retirement Account. Further, while the Civil Service Retirement law does permit voluntary contributions to purchase additional annuity, these contributions are not irrevocable, and there is no provision for the Federal Government as an employer to make contributions to an employee's voluntary contribution account.

H.R. 2 also provides for the study of Government pension plans by several Congressional committees (section 3031) to determine the adequacy of existing participation, vesting, funding, and fiduciary provisions of such plans. We will be pleased to cooperate with this study if requested.

Despite objections to several of the personnel provisions we recommend that the President sign enrolled H.R. 2. We view the provisions of this Act as being primarily designed to correct private employee pension plan deficiencies--which are not found in the Civil Service Retirement System. Our system has been open to all career employees and has had reasonably sound financing and reasonably early vesting provisions for some time. Nonetheless, the Commission will review the provisions of the enrolled enactment carefully to determine whether any provisions of the Civil Service Retirement System ought to be amended to conform the system to the new public policy enunciated for pension plans generally in the enrolled enactment.

By direction of the Commission:

Sincerely yours,

Robert Hampton

Chairman

DEPARTMENT OF HEALTH, EDUCATION, AND WELFARE

AUG 22 1974

Honorable Roy L. Ash
Director, Office of Management
and Budget
Washington, D. C. 20503

Dear Mr. Ash:

This is in response to Mr. Rommel's request of August 15, 1974, for a report on H.R. 2, the "Employee Retirement Income Security Act of 1974."

Under section 1032 of the bill the Secretary of Health, Education, and Welfare would be required to record information, received from the Secretary of the Treasury, concerning deferred vested benefit rights of pension plan participants who terminate employment covered by a plan. This information would include the name of the plan, name and address of the plan administrator, and the nature, amount, and form of the participants' vested benefits. (This information would be contained in annual statements required to be filed by plan administrators with the Treasury.) Beginning January 1, 1978, the Social Security Administration would report this information to plan participants upon request, or to the participant (or his dependents or survivors) automatically when he applies for social security benefits. The social security trust funds would be reimbursed from general revenues for administrative costs arising from the provision. We estimate that the amount of such administrative costs for the first two years (1978-1979) in which SSA would be required to report vested benefits rights would be approximately $4.8 million.

While we generally support this provision because we believe it would assist employees in remembering and locating the plans of former employers with whom they have vested rights, we have reservations concerning the requirement to record information as to the nature, amount, and form of the benefits promised by specific plans. Providing this information to plan participants would not result in any significant advantage to individuals with vested rights; a large part of the information would become outdated and unreliable since in many cases the value of vested rights is not a constant.

In spite of our reservations concerning the requirement for recording information as to the nature, amount, and form of vested benefits, we support the bill insofar as it affects this Department, and we recommend that the bill be approved.

Sincerely,

Secretary
Acting

THE GENERAL COUNSEL OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, D. C. 20410

AUG 23 1974

Mr. Wilfred Rommel
Assistant Director for
Legislative Reference
Office of Management and Budget
Washington, D. C. 20503

Attention: Mrs. Garziglia

Dear Mr. Rommel:

Subject: H.R. 2, 93d Congress, Enrolled Enactment

This is in response to your request for the views of this Department on the enrolled enactment of H.R. 2, the Employee Retirement Income Security Act of 1974.

This Department has no objection to approval of the enactment.

Sincerely,

Robert R. Elliott

Robert R. Elliott

UNITED STATES DEPARTMENT OF COMMERCE
The Assistant Secretary for Domestic and International Business
Washington, D.C. 20230

AUG 21 1974

Honorable Roy L. Ash
Director, Office of Management
and Budget
Washington, D.C. 20503

Attention: Assistant Director for Legislative Reference

Dear Mr. Ash:

This is in response to your request for the views of this Department with respect to H.R. 2, an enrolled bill to be cited as the

"Employee Retirement Income Security Act of 1974."

The Department of Commerce has no objection to approval by the President of H.R. 2.

Enactment of this legislation would not involve any increase in the budgetary requirements of this Department.

Sincerely,

Tilton H. Dobbin

Tilton H. Dobbin
Assistant Secretary for
Domestic and International
Business

ASSISTANT ATTORNEY GENERAL
LEGISLATIVE AFFAIRS

Department of Justice
Washington, D.C. 20530

AUG 22 1974

Honorable Roy L. Ash
Director, Office of
Management and Budget
Washington, D. C. 20503

Dear Mr. Ash:

In compliance with your request, I have examined the text of H.R. 2, the "Employee Retirement Income Security Act of 1974," as it appeared in the Congressional Record on August 12 and August 13, 1974.

The bill would protect the interests of participants in employee benefit plans and their beneficiaries by requiring the disclosure and reporting to participants and beneficiaries of financial and other information with respect to such plans; it would establish standards of conduct, responsibility, and obligation for fiduciaries of employee benefit plans; and it would provide for appropriate remedies, sanctions, and ready access to the Federal Courts. The bill further provides for vesting of accrued benefits of employees with significant periods of service and for employee benefit plans with termination insurance.

Although the Department of Justice supported the adoption by the conference of the litigating provisions now contained in Section 502 of H.R. 2, we did this only as a compromise of even more objectionable litigating provisions contained in the two versions of the bill at the time the bill went to conference. We have traditionally and will in the future oppose decentralization of the litigating authority of the Attorney General consistent with 28 U.S.C. §516-519 and OMB Circular No. A-99.

We have also consistently opposed one House resolution veto mechanisms such as those contained in Section 4002 and Section 4006 of H.R. 2. We submit that these provisions violate Article 1, Section 7 of the Constitution.

Subject to your consideration of the above observations, the Department of Justice defers to the Departments of Labor, Commerce and Treasury as to whether this bill should receive Executive approval.

Sincerely,

W Vincent Rakestraw
W. Vincent Rakestraw
Assistant Attorney General

THE WHITE HOUSE

ACTION MEMORANDUM WASHINGTON LOG NO.: 542

Date: August 28, 1974 Time: 9:15 a.m.

FOR ACTION:
✓ James Cavanaugh
✓ Geoff Shepard
✓ Phil Buchen
✓ Bill Timmons

cc (for information):
Warren K. Hendriks
Jerry Jones
Dave Gergen

FROM THE STAFF SECRETARY

DUE: Date: Thursday, August 29, 1974 Time: 2:00 p.m.

SUBJECT: Enrolled Bill H.R. 2 - Employee Retirement Income Security Act of 1974

ACTION REQUESTED:

___ For Necessary Action	XX For Your Recommendations
___ Prepare Agenda and Brief	___ Draft Reply
___ For Your Comments	___ Draft Remarks

REMARKS:

Please return to Kathy Tindle - West Wing

PLEASE ATTACH THIS COPY TO MATERIAL SUBMITTED.

If you have any questions or if you anticipate a delay in submitting the required material, please telephone the Staff Secretary immediately.

K. R. COLE, JR.
For the President

To - Warren Hendriks 8-27-74

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

AUG 27 1974

MEMORANDUM FOR THE PRESIDENT

Subject: Enrolled Bill H.R. 2 - Employee Retirement Income Security Act of 1974
Sponsors - Rep. Dent (D) Pennsylvania and Rep. Perkins (D) Kentucky

Last Day for Action

We believe that this bill should be acted on at the earliest possible time to minimize the possible cost impact of the termination insurance provisions of the bill, which are effective in part back to July 1, 1974.

Purpose

Establishes standards governing private pension plans, including reporting, disclosure, participation, vesting, funding, and fiduciary responsibilities, and authorizes a Pension Benefit Guaranty Corporation. (The administrative expense costs and the revenue loss from the tax provisions are summarized in a separate section near the end of this memorandum.)

Agency Recommendations

Office of Management and Budget	Approval
Department of Labor	Approval (Signing statement attached)
Department of the Treasury	Approval
Civil Service Commission	Approval
Department of Health, Education, and Welfare	Approval
Department of Housing and Urban Development	No objection
Department of Commerce	No objection
Department of Justice	Defers to other agencies

OPTIONAL FORM NO. 10
MAY 1962 EDITION
GSA GEN. REG. NO. 27

UNITED STATES GOVERNMENT

Memorandum

Department of the Treasury
Washington, D.C.

TO : Ralph Malvik, Legislative Analyst
Office of Management and Budget

DATE: August 27, 1974

FROM : Theodore E. Rhodes, Attorney Adviser TER
Office of Tax Legislative Counsel

SUBJECT: Points to be Included in President's Signing Statement

Attached is a revised copy of the Treasury's Points to be included in the President's Signing Statement. The principal changes made were in the introduction and the first paragraph of the background material. Would you please forward this to the White House.

Attachment