

FOIA MARKER

This is not a textual record. This is used as an administrative marker by the William J. Clinton Presidential Library Staff.

Collection/Record Group: Clinton Presidential Records
Subgroup/Office of Origin: National Economic Council
Series/Staff Member: Gene Sperling
Subseries:

OA/ID Number: 24558
FolderID:

Folder Title:
Labor - GI Bill / Job Training / Minimum Wage [3]

Stack:	Row:	Section:	Shelf:	Position:
S	16	5	7	2

THE WHITE HOUSE
WASHINGTON, D.C. 20500

DATE: 12-20

TO: Leon
George
Gene
Ruhnn
FROM: Staff Secretary

Leuch
Don

Fyi. I forwarded to
President.

Todd

MEMORANDUM FOR THE PRESIDENT

From: Robert B. Reich 
Date: December 18, 1995
Subject: Pensions

95 DEC 19 P4:15

Pension security should be one of your major themes. It ranks up there with Social Security and Medicare as a concern of working people. In the past three years the administration has accomplished a great deal to make pensions far more secure.

Overview

Approximately half of all working Americans in the private sector have pensions. More than 22 million are in 401(k) tax-deferred plans, in which they contribute from their own paychecks (about 3/4 of these workers have some part of their contribution matched by their employer). There are about 40 million participants and beneficiaries in private "defined benefit" plans, in which employers promise a specified pension when they reach retirement age. 401(k)s are growing quickly; defined benefit plans, provided mostly by large corporations, are declining as the proportion of employment in large firms shrinks.

Security of defined benefit plans

The problem here is that some companies fail to put aside enough money in their plans to fully fund their pension obligations when they come due. When you came to office, the problem of underfunding was growing dramatically. In 1987, underfunding amounted to \$27 billion. By the end of 1993, it was \$71 billion. The Pension Benefit Guarantee Corporation, which takes over the responsibility from underfunded plans, was going deeper into debt (I chair the PBGC). We didn't have a Savings and Loan situation on our hands, but it was heading in that direction.

The Pension Reform Act of 1994. Your Pension Reform Act changed all that. The law now requires that underfunded plans get on track toward full funding. We also put the spotlight of publicity on underfunded plans. Both of these initiatives, coupled with higher interest rates, turned the tide. The latest data show that underfunding has dropped to \$31 billion.

The Republican's current attack. Before 1990, companies with overfunded plans (i.e., more than enough money to pay pension obligations at the time) routinely used the surplus for their own purposes (typically for leveraged buyouts). This practice also threatened the integrity of the plans, because an overfunded plan at one point in time could become underfunded at a later point in time (if asset valuations and interest rates change). In 1990, Congress closed that barn door by imposing a high excise tax on the use of any such surplus.

Now, the Republican budget plan seeks to reopen that barn door. By the Republicans' own estimate, corporations would remove from their plans about \$15-18 billion over the next 5 years. You are opposing this.

Security of 401(k) plans

Over 22 million working people save through 401(k) pension plans (up from around 7 million just ten years ago). There are now more than 150,000 such plans, with more than \$600 billion in assets.

Enforcement crack-down. The vast majority of 401(k) plans are secure. During the last year, however, the Department of Labor has received a number of complaints from employees about employers who allegedly have failed to deposit in the plans employee 401(k) contributions withheld from paychecks. An unusually high percentage of such complaints have resulted in civil and criminal actions. The Department has opened over 400 cases and recovered more than \$3.5 million for 2,800 workers to date. Some cases have been turned over to federal and state prosecutors; several employers have been found guilty and await sentencing.

As a result of the Department's enforcement actions, the issue has received significant coverage in recent weeks, including all network morning and evening news programs, as well as all major print media (see attached sample clips). We have emphasized the importance of employee awareness, while also assuring employees that the vast majority of 401(k) plans are secure.

Additional steps to secure 401(k)s

In addition to our enforcement and public-awareness efforts, we are pursuing three other means of safeguarding 401(k) pensions:

1. Tightening the rules on speedy deposits. Last week (December 11), we announced that you had asked me to propose to reduce the maximum amount of time that employers can hold their employees' 401(k) savings before depositing the money into an employee benefit plan. Under current regulations, employers must

deposit as soon as possible but no later than 90 days from the date of withholding. We have had a number of reports of employers routinely holding the contributions for the full 90 days, treating them as a kind of permanent tax-free loan fund. The proposed rule would require that employers deposit employee 401(k) contributions on the same schedule that payroll taxes must be forwarded to the Internal Revenue Service. After a comment period, we expect a new rule to be in place within 90 days.

2. Requiring accountants to report fraud. Last July, the Administration sent to Congress the "ERISA Enforcement Improvement Act," which would, among other things, require accountants to report immediately to the Labor Department any evidence of serious plan fraud. On December 7, 1995, you wrote to congressional leaders urging swift approval. We expect Senators Jeffords and Simon to introduce the legislation this week. There is considerable bi-partisan support.

3. Amnesty. Finally, we're discussing with Treasury and Justice a possible "amnesty" period during which employers could restore delinquent 401(k) deposits without penalty. This is on track for announcement between Christmas and New Year. The timing of this announcement could be affected by the government shutdown.

Your visibility on pension security

You have had some visibility on various of these pension security issues, but the overall story has not been told. The administration should get more credit. You might consider a place in the State of the Union, or a separate free-standing speech.

Pension security fits nicely within an overall theme emphasizing the importance of ensuring that all Americans enjoy the fruits of their hard work--coupling opportunity and responsibility, linking American work with the American dream.

7 pages total

September 14, 1995

MEMORANDUM FOR GENE SPERLING
TOM O'DONNELL

FROM: Ellen Seidman

SUBJECT: Archer Pension Raid Proposal

Section 13607 of Chairman Archer's bill (page 127), described in item 9 of the summary (page 15), would allow employers to take money out of marginally over-funded pension plans "for any purpose." This is a blatant raid on workers' pension money, and goes entirely contrary to what Congress achieved in the Retirement Protection Act, passed as part of GATT last December, which was meant to ensure that employers would fund their pension plans and keep their promises to their employees.

IT IS CRITICAL THAT WHATEVER STATEMENT THE PRESIDENT MAKES BLASTING THE ARCHER PACKAGE INCLUDES A CLEAR AND UNAMBIGUOUS REJECTION OF THIS PROPOSAL.

In the 1980s, over \$20 billion was taken out of pension plans through "reversions." When the economy and corporate fortune turned at the end of the decade, many of those plans were left underfunded, which led Congress to stop the raid. This proposal would start it all over again.

It is not only lousy retirement policy, it is lousy tax policy (it enables rich employers to use their pension plans as a tax shelter).

Archer will justify the proposal on the grounds that the plans would still be overfunded. However, the assumptions used in calculating whether they would be have been shown by the PBGC to significantly understate what would be needed to pay workers if the plan terminated. And the GAO found that even the PBGC calculation underestimates what happens in the real world when a company gets into financial trouble and has to terminate its pension plan.

The AFL-CIO was lobbying heavily against an earlier rumored version of this proposal, which would have limited the use of the pension money to health care. They are presumably going ballistic now. Mr. Gibbons blasted the proposal on the floor this evening. Alice Rivlin also sent up a letter on the earlier version.

Attached are:

- o Archer's description of the provision
- o Alice's letter
- o A short rhetorical diatribe on the provision that could be used by the President, Gephardt or someone else

09/14/95 THU 18:55 FAX 202 326 4016

PBGC/OED

004

transfer of excess assets from a defined benefit pension plan (other than a multiemployer plan) to the employer. Amounts transferred could be used by the employer for any purpose. Amounts transferred would be includible in the gross income of the employer and generally would be subject to a 6.5-percent excise tax. No excise tax would apply in the case of transfers occurring before July 1, 1996.

A transfer would not affect the plan's qualified status and would not be considered a prohibited transaction. There would be no limit on the number of such transfers that could be made during any taxable year.

In order for the transfer to be qualified, the accrued retirement benefits of participants (including participants who separated from service during the 1-year period ending on the date of the transfer) under the pension plan must be nonforfeitable as if the plan terminated immediately before the transfer. The other requirements under present law for qualified transfers to pay qualified current retiree health liabilities (e.g., the maintenance of effort requirement) generally would not apply.

Excess assets would be defined as under present law, and would be determined as of January 1, 1995, or, if January 1, 1995, is not a plan valuation date, as of the last plan valuation date preceding January 1, 1995.

The proposal would not apply to transfers in taxable years beginning after December 31, 2000.

Effective Date

The proposal would be effective January 1, 1995.

10. Modify tax benefits for ethanol and methanol from renewable sources

Present Law

Present law provides several tax benefits for ethanol and methanol produced from renewable sources (e.g., biomass) that is used as a motor fuel or that is blended with other fuels (e.g., gasoline) for such a use. These benefits are--

(1) A 54-cents-per-gallon (60 cents per gallon for methanol) blender income tax credit;

(2) A 5.4-cents-per-gallon (6 cents per gallon for methanol) excise tax exemption from the motor fuels excise taxes; and

(3) In the case of ethanol, a separate 10-cents-per-gallon credit for small producers, defined generally as persons whose production does not exceed 15 million gallons per year

09/14/95 THU 18:54 FAX 202 328 4016

PBGC/OED

003

Upon plan termination, the accrued benefits of all plan participants are required to be 100-percent vested.

Under present law, a pension plan may provide medical benefits to retirees through a section 401(h) account that is part of such plan. Present law permits certain qualified transfers of excess assets from the plan assets in a defined benefit pension plan (other than a multiemployer plan) to a section 401(h) account that is part of such plan to pay for qualified current retiree health liabilities (sec. 420). Such a transfer does not affect a plan's tax-qualified status and is not a prohibited transaction (sec. 4975). Further, the assets transferred are not includible in the gross income of the employer and are not subject to the excise tax on reversions. Only one qualified transfer with respect to a plan may be made during a taxable year.

Qualified transfers must satisfy several requirements and the assets transferred must not exceed certain limits. Under one of these requirements, the accrued retirement benefits of participants (including participants who separated from service during the one-year period ending on the date of the transfer) under the pension plan must be nonforfeitable as if the plan terminated immediately before the transfer. In addition, the transferred assets (and any income thereon) are required to be used to pay qualified current retiree health liabilities (either directly or through reimbursement) for the taxable year of transfer. Transferred amounts are generally required to benefit all participants in the pension plan who are entitled upon retirement to receive retiree medical benefits (other than key employees) through the section 401(h) account. Amounts not used to pay qualified current retiree health liabilities for the taxable year of the transfer must be returned at the end of the taxable year to the general pension assets of the plan. Under a so-called maintenance of effort requirement, the employer is required to maintain current health benefit levels for a period of time after the transfer.

Only excess assets may be transferred under section 420. Excess assets are defined to be the excess of the value of plan assets (calculated as under the full funding limitation) over the greater of (1) the lesser of (a) 150 percent of current liability or (b) the accrued liability under the plan, or (2) 125 percent of current liability. For example, in the case of a plan subject to the accrued liability full funding limitation, the value of assets remaining in the plan following a transfer must be at least the greater of the plan's accrued liability or 125 percent of current liability. The calculation of excess assets is generally made as of the most recent valuation date preceding the transfer.

The provision permitting qualified transfers of excess pension assets to pay qualified current retiree health liabilities expires for taxable years beginning after December 31, 2000.

Description of Proposal

The proposal would provide an additional method under which employers could transfer excess assets from a defined benefit plan. The proposal would permit a qualified

09/14/95 THU 18:53 FAX 202 328 4016

PBGC/OED

Description of Proposal

The proposal would provide that where the taxpayer satisfies the replacement property requirement of section 1033 by acquiring stock in a corporation, the corporation generally would reduce its adjusted bases in its assets by the amount by which the taxpayer reduces its basis in the stock. The corporation's adjusted bases in its assets would not be reduced, in the aggregate, below the taxpayer's basis in its stock (determined after the appropriate basis adjustment for the stock). In addition, the basis of any individual asset would not be reduced below zero. The basis reduction first would be applied to (1) property that is similar or related in service or use to the converted property, then (2) to other depreciable property, then (3) to other property.

The application of these rules can be demonstrated by the following examples:

Example 1.--Assume that a taxpayer owned a commercial building with an adjusted basis of \$100,000 that was involuntarily converted, causing the taxpayer to receive \$1 million in insurance proceeds. Further assume that the taxpayer acquires all of the stock of a corporation, the sole asset of the corporation is a building with a value and an adjusted basis of \$1 million, and the stock acquisition qualifies as the acquisition of replacement property. Under the proposal, for section 1033 to apply, the taxpayer would reduce its basis in the stock to \$100,000 (as under present law) and the corporation would reduce its adjusted basis in the building to \$100,000.

Example 2.--Assume the same facts as in Example 1, except that on the date of acquisition, the corporation has an adjusted basis of \$100,000 (rather than \$1 million) in the building. Under the proposal, the taxpayer would reduce its basis in the stock to \$100,000 (as under present law) and the corporation would not be required to reduce its adjusted basis in the building.

Effective Date

The proposal would apply to involuntary conversions occurring after September 13, 1995.

9. Corporate pension reversions

Present Law

Under present law, defined benefit pension plan assets generally may not revert to an employer prior to the termination of the plan and the satisfaction of all plan liabilities. Any assets that revert to the employer upon such termination are includible in the gross income of the employer and subject to an excise tax (sec. 4980). The rate of the excise tax generally is 20 percent, and is increased to 50 percent unless the employer maintains a replacement plan or makes certain benefit increases in connection with the plan termination.



THE DIRECTOR

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET

WASHINGTON, D.C. 20503

September 13, 1995

The Honorable Bill Archer
Chairman, Committee on Ways and Means
United States House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

It is my understanding that Congress may be asked to allow companies to take funds out of pension plans and use them to pay health benefits for active workers or for other purposes by amending Section 420 of the Internal Revenue Code. I urge you to reject such an amendment.

Section 420 now allows an employer to transfer assets tax-free from a defined benefit pension plan to a health benefits account to pay health care costs for retirees. These assets continue to be used for retirement expenses. Companies are asking that they be given these same advantages when transferring assets to pay the health care costs of active workers or to pay other employer costs.

Allowing companies to use pension assets in this manner is contrary to the most fundamental principles of the Employee Retirement Income Security Act of 1974. The transfer would not be for retirement purposes. It carries the potential for a repeat of the large pension raids of the 1980s, when over \$20 billion was taken out of plans through "asset reversions."

The proposed amendment will also increase the risk of loss to the pension insurance system. Section 420 requires that the assets remaining in the plan equal at least 125 percent of the plan's "current liability," to assure that the plan can pay benefits over time if it remains ongoing. Companies can make this calculation using actuarial assumptions that would leave a pension plan underfunded if it is terminated. Analysis shows that a transfer consistent with the proposal could nevertheless leave a plan with less than 90 percent of the funds needed for termination payments.

This is particularly disturbing in light of the December 1992 study by the General Accounting Office, "Pension Plans: Hidden Liabilities Increase Claims Against Government Insurance Programs." The GAO study demonstrates that the financial situation of many pension plans deteriorates significantly prior to their termination. A company

09/14/95 THU 19:11 FAX 202 326 4016

PBGC/OED

008

- 2 -

could transfer assets under the Section 420 proposal, suffer an economic reversal, and then terminate its plan with a funding level that falls well below 90 percent. A company ~~might well have an incentive to make such a transfer.~~ Giving companies a way sharply to reduce assets in their pension plans will increase the risk of loss for plan participants and the PBGC.

Last year, on a bipartisan basis, Congress passed the Retirement Protection Act of 1994, shoring up pension funding and the PBGC. Broadening Section 420 could undermine the purpose of the Retirement Protection Act, and risks eroding confidence in our private retirement system. The Administration strongly opposes such a broadening and urges you not to include it in any legislation.

Sincerely,



Alice M. Rivlin
Director

THE WHITE HOUSE
WASHINGTON

March 11, 1996

MEMORANDUM FOR THE PRESIDENT

FROM: LAURA D'ANDREA TYSON

SUBJECT: Attached memo from Secretary Reich concerning
pension portability

While your pension simplification and IRA proposals go a long way toward increasing pension coverage and portability, as Secretary Reich's memo points out, barriers remain to complete portability of even defined contribution plans -- mainly 401(k) plans. For example, while employers routinely allow departing workers to roll 401(k) accounts into IRAs or into a subsequent employer's 401(k) plan, the IRA rules are complex and many employers will not accept the rollovers.

Secretary Reich's memo raises the question whether a revised, repackaged pension coverage/portability proposal could include statutory and regulatory provisions to reduce these barriers. Along with Secretary Reich, I believe the answer is "yes."

For the past several months, the NEC pension working group -- which includes active participation from the Labor Department -- has been developing such a revised pension coverage/portability proposal. The items raised in Secretary Reich's memo are under discussion, and various ways of dealing with the problems raised without creating new problems for either employers or employees are being developed. Thus, I believe no additional response to Secretary Reich's suggestion is needed at this time.

We hope to be able to present a broader revised proposal that includes these new items to you within the next several weeks.

SECRETARY OF LABOR
WASHINGTON

MAR 1 1996

MEMORANDUM FOR THE PRESIDENT

FROM: ROBERT B. REICH *Rb*
THROUGH: LAURA TYSON
SUBJECT: PENSION PORTABILITY

Herewith, a number of ideas for making 401(k) pensions more portable.

As you know, over 20 million Americans now save at work through 401(k) plans, and the numbers are growing quickly (approximately twice that number are in traditional "defined benefit" plans, but their numbers have remained constant as employers increasingly offer 401(k)s, and as large firms downsize).

401(k) plans are "portable" in the limited sense that workers who leave their jobs typically can roll over their 401(k)s to an IRA and sometimes to a new employer plan. However, pension law gives workers little control over many aspects of portability. For example, job-to-job portability is not possible for about half of all workers because pension law does not require employers who offer plans to accept transfer of their employers' 401(k) savings from previous employment.

Further, the option of rolling a 401(k) to an IRA is more difficult than it may appear. To avoid tax penalties, workers must tip toe their way through tax and timing issues and may have to retain multiple accounts in order to preserve retirement savings or transfer to future employers' plan.

The attached provisions would go some way towards providing more meaningful portability for workers. They could be combined with the pension simplification package already in your budget or included in a later pension initiative. It is my understanding that the NEC is considering these and other ideas.

Attachment

401(k) PLAN PORTABILITY ISSUES

I. BACKGROUND

Pension portability is complicated and is related to other important considerations, such as coverage and benefit adequacy. The challenge is to find ways to expand portability and coverage for workers, while balancing the costs and administrative burdens on employers in a voluntary pension system.

Significant portability changes in defined benefit plans would require radical reforms and could raise costs so as to discourage defined benefit plans.¹

In the 401(k) setting, portability means the ability of workers to preserve retirement savings following a change in employment. 401(k) plans are now relatively portable because workers who separate from jobs may under many circumstances transfer their 401(k) accounts to IRAs or other employers' pension plans.

II. ANALYSIS OF ISSUES

A. 401(k) PLANS ARE NOT REQUIRED TO ACCEPT ROLLOVERS

Issues

When a worker changes jobs, the law allows direct transfers from one employer's 401(k) plan to an IRA or another employer's plan that chooses to accept transfers.

An estimated 98 percent of 401(k) participants are in plans that offer direct transfers for workers who separate before retirement. There is no requirement for 401(k) plans to accept transfers and only 51 percent of 401(k) participants are in plans that do so.

¹Defined benefit plans are designed to fund benefits payable over thirty to forty years, generally on the highest salary. An employer hiring an older worker would assume disproportionate costs for the benefits promised from previous employment. Furthermore, since defined benefit plans count on compounding to fulfill their eventual obligations, the withdrawal of assets would have a detrimental effect on the financial status of the funds.

A direct transfer to an IRA is an alternative for workers unable to rollover their 401(k)s to a new employer's plan. A 401(k) distribution can be transferred directly to a conduit IRA, and later transferred to another 401(k) plan, but this arrangement is not as simple as it appears. Funds in a conduit IRA may be transferred tax-free to another 401(k) plan only if it is not commingled with regular IRA assets. A worker has to establish a second IRA account to receive 401(k) distributions. As contrasted with 401(k) accounts, IRAs may be subject to the claims of creditors.

For those workers fortunate to find a new employer plan that accepts transfers, the receiving plan may be able to delay such a transfer until workers satisfy a waiting period which can be as long as two years. In order to make a requirement that plans accept rollovers a real option, workers should be able to roll their previous accounts of any amount over into a new employer plan even if they are not participating yet in that plan.

Option

Require 401(k) plans to accept direct transfers, possibly before a new worker would be eligible to participate in the plan.

Pros

The consolidation of saving accounts simplifies workers' retirement planning and investment decisions. Requiring plan sponsors to accept rollovers would reduce leakage due to lump sum cashouts.

Cons

Plan sponsors would object to the added administrative burdens and to accepting transfers before a new employee starts participating in the plan because turnover is relatively high for probationary employees.

B. CREATE NEW OPTIONS FOR WORKERS CHANGING JOBS

Issues

Most plans impose a waiting period for new employees. Employers impose waiting periods because they have high turnover among their low-paid employees and probationary employees. Employees who stay for only a short period of time are the least likely to contribute to 401(k) plans. If these employees were eligible for the plan, their failure to contribute would reduce the averages used to determine how much the highly-compensated employees may contribute.

Thus, an employee who switches jobs is often unable to continue uninterrupted 401(k) savings. At the same time, employees who were covered by the prior employer's plan or whose spouse has pension coverage may be unable to make tax-deductible contributions to an IRA.

Option 1

Allow 401(k) plans to accept employee salary deferrals during the period before a new employee is eligible to participate in the plan, without subjecting those contributions to discrimination testing.

Pros

Allowing plans to accept employee contributions would encourage continued savings among workers who change jobs. This proposal is a complement to the option discussed in issue A. If both options were adopted, employees may be able to consolidate their 401(k) savings as well as continue to contribute.

Cons

Highly-paid employees are more likely to take advantage of this option than low-paid employees. Plan sponsors may object to setting up and maintaining 401(k) accounts for short service employees.

Option 2

Allow employees who change jobs to contribute to an IRA during the period before they are eligible to participate in their new employer's plan.

Pros

Allowing IRA contributions would encourage continued savings among workers who change jobs.

Cons

Highly-paid employees are more likely to contribute, since only they are restricted from making tax-deductible contributions to IRAs.

C. WORKERS CANNOT CONTROL THE TIMING OF DISTRIBUTIONS OR ROLLOVERS

Issues

Workers have reported that they have little control over the timing of their 401(k) distributions and transfers. Typically participants can elect to (1) have the retirement savings directly transferred to another retirement account; (2) take the 401(k) assets in a lump sum; or (3) leave the assets in the 401(k) plan until retirement. We have little evidence that timing is a widespread problem, but there are two issues to consider:

1. **Workers are required to make hasty elections:** Workers leaving jobs may only have a short period of time within which to make decisions about direct transfers. Workers facing long waiting periods to participate in a new employer plan would benefit from having the ability to elect a direct transfer at a later date after separation.

Option 1

Require plans to permit separating workers to elect direct transfers at any time after separation.

Pros

Allowing workers to better control the timing of transfers would mean that they would not have to maintain multiple savings accounts.

Cons

There is not much evidence to show that this is a widespread problem.

2. **Workers face significant delays in getting access to their 401(k) assets:**

Some workers have complained that once they have elected to transfer or cashout their 401(k) plan assets, they experience significant delays in having those decisions acted upon by the plan. Plans may postpone the distribution of 401(k) accounts until the next valuation of plan assets in order to properly allocate earnings to all participants. Surveys show that most plans conduct quarterly valuations.

Option 2

Require plans to make distributions no later than a set time after valuations unless the employee has elected a later date.

Pros

Workers who are leaving their jobs benefit from a clear standard in the law that sets a maximum period of time for distributions to be made after valuations. Focusing on the timing of distributions rather than the frequency of valuation would not require plans to make major changes in the way they operate.

Cons

Again, we do not have evidence of a widescale problem.

D. PROHIBITING INVESTMENT OPTIONS BASED ON EMPLOYMENT STATUS

Issues

Many participants do not transfer their 401(k) accounts because they prefer other forms of distribution such as an annuity or lump sum. We estimate that of the total \$22 billion in pre-retirement distributions, \$10 billion in 401(k) assets were spent in 1995 rather than saved for retirement.

If the plan provides that 401(k) assets must remain in the plan until retirement age unless immediate distribution is taken, separating workers may be encouraged to take a pre-retirement cash-out. Some plans may encourage cash-outs by providing fewer investment options for separated participants than for active workers.

Option

Require plans to offer the same investment options to all participants regardless of their status.

Pros

This eliminates a disincentive and encourages workers to keep their retirement savings in their 401(k) accounts.

Cons

Without a record of abuse in this area, employers may see the imposition of this rule as unnecessary.

E. ALLOWING TRANSFERS OF AFTER-TAX SAVINGS TO IRAs

Issues

The tax code does not allow after-tax contributions in a 401(k) plan to be transferred or rolled over to another tax-favored vehicle. This means that a worker who consolidates retirement savings loses the ability to shelter the income on after-tax amounts from taxation, resulting in lower savings at retirement.

Option

Allow the transfers of after-tax amounts to IRAs.

Pros

Workers gain the ability to shelter the income of after-tax amounts from taxation as well as simplicity.

Cons

The transfer of after-tax contribution to IRAs may require complicated recordkeeping for tax purposes.

MEMORANDUM FOR

From: Robert B. R

Date: December 11

Subject: Pensions

Per Todd Stern's
Instruction this
Attachment was
not forwarded to
Potus. It had
been previously
forwarded to Potus
in December

25 DEC 19 P4:15

typical fund ill for
DBB - pre-fund provided
Said if underfunded -- how pay
higher premiums. Enforce more strictly
Sew a system to help city w

Pension security should be one of your major themes. It ranks up there with Social Security and Medicare as a concern of working people. In the past three years the administration has accomplished a great deal to make pensions far more secure.

Overview

Approximately half of all working Americans in the private sector have pensions. More than 22 million are in 401(k) tax-deferred plans, in which they contribute from their own paychecks (about 3/4 of these workers have some part of their contribution matched by their employer). There are about 40 million participants and beneficiaries in private "defined benefit" plans, in which employers promise a specified pension when they reach retirement age. 401(k)s are growing quickly; defined benefit plans, provided mostly by large corporations, are declining as the proportion of employment in large firms shrinks.

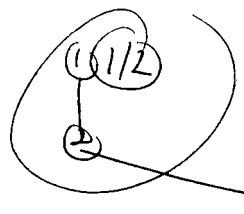
Security of defined benefit plans

The problem here is that some companies fail to put aside enough money in their plans to fully fund their pension obligations when they come due. When you came to office, the problem of underfunding was growing dramatically. In 1987, underfunding amounted to \$27 billion. By the end of 1993, it was \$71 billion. The Pension Benefit Guarantee Corporation, which takes over the responsibility from underfunded plans, was going deeper into debt (I chair the PBGC). We didn't have a Savings and Loan situation on our hands, but it was heading in that direction.

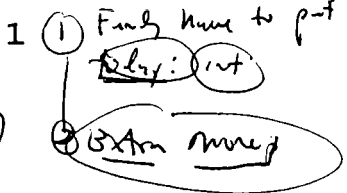
The Pension Reform Act of 1994. Your Pension Reform Act changed all that. The law now requires that underfunded plans get on track toward full funding. We also put the spotlight of publicity on underfunded plans. Both of these initiatives, coupled with higher interest rates, turned the tide. The latest data show that underfunding has dropped to \$31 billion.

Decker (1994)
Laws up-til
now: Dam good
choice for:

TWA



Funds of two to
Interest rates up in 1994
Funds have to put away today



Save 8
million per

underful pension - plan w/ 8 mil in
was underful

= not sy under

This part for me (8 mil)
in - who for ~~was~~ many will
under ppl

you can't

ERs

The Republican's current attack. Before 1990, companies with overfunded plans (i.e., more than enough money to pay pension obligations at the time) routinely used the surplus for their own purposes (typically for leveraged buyouts). This practice also threatened the integrity of the plans, because an overfunded plan at one point in time could become underfunded at a later point in time (if asset valuations and interest rates change). In 1990, Congress closed that barn door by imposing a high excise tax on the use of any such surplus.

Now, the Republican budget plan seeks to reopen that barn door. By the Republicans' own estimate, corporations would remove from their plans about \$15-18 billion over the next 5 years. You are opposing this.

Security of 401(k) plans

Over 22 million working people save through 401(k) pension plans (up from around 7 million just ten years ago). There are now more than 150,000 such plans, with more than \$600 billion in assets.

Enforcement crack-down. The vast majority of 401(k) plans are secure. During the last year, however, the Department of Labor has received a number of complaints from employees about employers who allegedly have failed to deposit in the plans employee 401(k) contributions withheld from paychecks. An unusually high percentage of such complaints have resulted in civil and criminal actions. The Department has opened over 400 cases and recovered more than \$3.5 million for 2,800 workers to date. Some cases have been turned over to federal and state prosecutors; several employers have been found guilty and await sentencing.

As a result of the Department's enforcement actions, the issue has received significant coverage in recent weeks, including all network morning and evening news programs, as well as all major print media (see attached sample clips). We have emphasized the importance of employee awareness, while also assuring employees that the vast majority of 401(k) plans are secure.

Additional steps to secure 401(k)s

In addition to our enforcement and public-awareness efforts, we are pursuing three other means of safeguarding 401(k) pensions:

1. Tightening the rules on speedy deposits. Last week (December 11), we announced that you had asked me to propose to reduce the maximum amount of time that employers can hold their employees' 401(k) savings before depositing the money into an employee benefit plan. Under current regulations, employers must

tax deduct now
intervention
tax deferral

Very light

81 mil¹ elyht

81 m mil for 100

16 million

100 million

81 m. ltr

SIMPLE

~~to~~
tens of millions

① have access to actions sy p¹ - DC
- per plan of any sort.
DB

② - Why: of kts can for a small
(Brow. the red tape, the Adm etc)
for 420

③ ~~With~~ 2 hundred a Copress a plan
Full open house of Act in
to work with only
1 pge form. 2A and
then are for tens of million.

do
faster

deposit as soon as possible but no later than 90 days from the date of withholding. We have had a number of reports of employers routinely holding the contributions for the full 90 days, treating them as a kind of permanent tax-free loan fund. The proposed rule would require that employers deposit employee 401(k) contributions on the same schedule that payroll taxes must be forwarded to the Internal Revenue Service. After a comment period, we expect a new rule to be in place within 90 days.

2. Requiring accountants to report fraud. Last July, the Administration sent to Congress the "ERISA Enforcement Improvement Act," which would, among other things, require accountants to report immediately to the Labor Department any evidence of serious plan fraud. On December 7, 1995, you wrote to congressional leaders urging swift approval. We expect Senators Jeffords and Simon to introduce the legislation this week. There is considerable bi-partisan support.

3. Amnesty. Finally, we're discussing with Treasury and Justice a possible "amnesty" period during which employers could restore delinquent 401(k) deposits without penalty. This is on track for announcement between Christmas and New Year. The timing of this announcement could be affected by the government shutdown.

Your visibility on pension security

You have had some visibility on various of these pension security issues, but the overall story has not been told. The administration should get more credit. You might consider a place in the State of the Union, or a separate free-standing speech.

Pension security fits nicely within an overall theme emphasizing the importance of ensuring that all Americans enjoy the fruits of their hard work--coupling opportunity and responsibility, linking American work with the American dream.

Dr

Auth is so much in cyph. missing

missing

① Problem: that some ERs
not going (in to)
one guest

Handy
Missus
for a long

for, he is hard
with some AER
no longer he is

③

- 400 ways in lot or not
- issue new reg speed up
not too the up
- new skil of acct rpt to op
And while ~~at~~
money is still M

③

tight timetable - we will
be and be done
Best way to get it done
+ payroll

Gene S

THE PRESIDENT HAS SEEN

1-4-96

96 JAN 3 48:47

THE WHITE HOUSE
WASHINGTON

January 2, 1995

MEMORANDUM FOR THE ~~PRESIDENT~~

FROM: LAURA TYSON *Laura Tyson*
RE: REICH MEMO ON PENSIONS

I agree wholeheartedly with Bob's view that pension security should be a key issue for 1996 and that you should get more credit for what your Administration has already accomplished in this area. I believe this issue deserves a place in the State of the Union. As I mentioned in an earlier memo to you, as part of your 1996 emphasis on pension security, you might also consider creating a Blue-Ribbon private-sector advisory commission on pension security and social security reforms. You will recall that Eli Broad has strongly recommended such an approach in earlier communications with you.

2 agree

1 agree with

cc: Leon

THE WHITE HOUSE

WASHINGTON

August 7, 1995

MEMORANDUM TO THE PRESIDENT

FROM:

LAURA TYSON

Laura D. Tyson

RE:

YOUR LETTER TO ELI BROAD ON RETIREMENT SAVINGS

Like you, I was very impressed by Mr. Broad's clear and compelling presentation on our nation's retirement savings challenge at the Pacific Rim Economic Conference. I think his idea of an independent bipartisan commission to develop a national retirement savings plan is a promising one. The State of the Union speech might provide a good opportunity for announcing the formation of such a commission. In the meantime, the NEC will examine several proposals to increase savings, including those recommended by Mr. Broad, in its review of tax reform alternatives which should be completed this fall. If you would like any more information before you send your letter to Mr. Broad, please let me know.

2nd
The pr: don't let y for pl, with for
+ pr: with

products power
enough to
fully full

products & small w
shop for with
net on at 11/14
bully interest

Person Supplement:

- Firm w/ 1000 + more 73% DB
- For 100 + firm + 23%

have not access
to not person

pl - complaint

Complex: Deal with
h, h

Small Dams like ZRA

Chap -
- Am - report
File I form

NEST

With B&B

→ Headline: Family aggregation

April 2, 1996

MEMORANDUM FOR: LAURA TYSON
FROM: GENE SPERLING
ELLEN SEIDMAN
SUBJECT: Pension reversion provision in new pension package

The Issue

During the 1980s, pension reversions were used by many companies to finance mergers, acquisitions, leveraged buyouts and for general corporate purposes. Pension plans sponsored by some of these same companies later became severely underfunded, to the detriment of workers and retirees. In 1990, Congress enacted a set of excise taxes, at levels as high as 50%, to recapture the tax benefits to corporations of funding pension plans. The excise taxes have virtually eliminated reversions, although withdrawals are allowed for retiree health expenses. During the 1995 budget battle, the Republicans proposed to sharply increase the ability of corporations to take reversions for general corporate use without paying the excise tax.

The Administration vigorously fought the Republican proposals to cut back substantially on the 1990 limitations, characterizing them as "pension raiding," and citing the excesses of the 1980s. Although the proposal was eliminated in the Senate, it was included in the final Balanced Budget package, and was cited as one of the reasons for the President's veto. The public response to the Administration's position was extremely favorable.

What Next? - Options

We would like to revive and replay the reversions issue as part of a proposed pension initiative. There are four options for doing this:

- Propose nothing new, but characterize the new package as consistent with and building upon the Administration's opposition to pension raiding, relying on rhetoric rather than a proposal to revive the issue.
 - The Administration's stand against reversions, and the characterization of the Republicans' proposal as "pension raiding," is well-known and has been successful. Simply reminding people of it will have resonance.
 - The 1990 changes have solved the problem of 1980s-style abuse; nothing more is needed.
 - To some extent, the limited right to take a reversion, even with penalties, helps encourage employers to fully fund their plans, because they know they can have access to the excess if it is really needed.
 - Although business supported the Republican proposal, they were somewhat embarrassed by it and did not overtly oppose the Administration's position; going further may generate overt opposition.
 - Making a new proposal will focus the debate on the merits of that proposal, rather than keeping it focused on the Republican's error.
- Propose amending the law to require the Treasury or Labor Department to report annually to Congress on reversion activity since the enactment of ERISA, and to supplement the report annually.
 - By proposing some change, we increase the focus on this issue and on our position against Republican "pension raiding."

- A report could demonstrate that the current law's excise taxes have been effective in preventing reversions and serve as a periodic reminder of Republican efforts to raid pensions.
 - A reporting requirement of this sort is unlikely to generate opposition, change the terms of the debate, or create other significant risks.
 - However, such a report will do little to increase the disincentives for individual companies to take reversions.
- Propose amending the law to require employers who take reversions to give notices to their employees before such action is taken.
 - By proposing a change focused on employees, we increase the focus on the employee-protection aspects of this issue and on our position in contrast to Republican pension raiding.
 - Having to provide such a notice can be a significant disincentive to taking a reversion.
 - However, by proposing such a notice requirement, we may imply that (i) reversions are fine, as long as employees are told and (ii) far more reversions are taking place than is in fact the case, potentially creating unnecessary worry on the part of employees.
 - Businesses are likely to view this type of reporting requirement as a practical limit on their ability to take reversions, which may create overt opposition to the Administration's position where little now exists.
 - It may have some impact on business's desire to fully fund plans – and will certainly lead to their stating that it will have such an impact.
 - Propose amending the law to prohibit reversions entirely.
 - This is an unambiguous further statement of our opposition to Republican pension raiding.
 - This will establish by implication what has long been ambiguous: that money in a pension trust belongs to the employees, not the employer.
 - The ownership issue is, however, one of the clearest "hot buttons" for employers; to raise it now will divert attention from the good things in our package and virtually assure business opposition.
 - Reversions have in fact been held to a trickle by the stiff excise taxes imposed in 1990; to propose to prohibit them entirely may imply that they are more common than is the case, thereby unnecessarily generating employee concern.
 - Current law helps encourage full funding by allowing employers the possibility of recovering excess funding after payment of all benefits and excise taxes. Small business owners already complain that, if they fund generously, they are particularly exposed to the risk that there will be excess assets on plan termination that will be largely taxed away. Both small and large business will assert that a reversion ban will discourage them from adequately funding pension plans.
 - Including a total ban on reversions in a message focused in part on alleviating the impact of downsizing invites the question why we should preclude completely any possibility that a financially strapped company with sufficient pension surplus might choose to withdraw the surplus to save workers' jobs.
 - We have had fairly good bipartisan support for our position; the Senate vote to delete the reversion provision was 94-5. This would polarize the issue, and may carry the polarization over to the broader issue of pension reform, which has long enjoyed solid bipartisan support.

Recommendation

We understand the Secretary of Labor favors the fourth option, an outright ban. We understand the Secretary of Treasury is opposed to such a ban on both policy and political grounds, and is not convinced of the need to take any legislative action. We recommend the second option -- a Treasury or Labor report on reversions. It is important to use this legislation to express strongly that we must not go backwards on reversions, and having a legislative hook that says we'll put the spotlight on any increase in reversion activity is sufficient to accomplish this, without generating unneeded opposition.

DRAFT

April 3, 1996

MEMORANDUM FOR THE PRESIDENT

FROM: GENE SPERLING

SUBJECT: Pensions initiative for your interview with E.J. Dionne today

I [and others?] recommend that you discuss with E.J. Dionne today the pension package that you will be announcing next Tuesday, April 9. We have not yet announced it to the press or the Hill; Dionne's column will come out the day of the event.

The Problem: Millions of Americans worry that they will not have enough money to maintain their standard of living when they retire and will be a burden on their children. Too many Americans are not covered by a pension plan and find saving for retirement an incomprehensible maze. Or if they are lucky enough to be covered by an employer-provided pension plan, they worry that their pension funds are not secure, and face an obstacle course to take their retirement savings with them when they change or lose their job.

Your Pension Package: Your pension package builds on your pension simplification and IRA proposals to make it easier to save for the future, easier to take your savings with you when you change or lose jobs, and ensure that people's retirement savings are safe and there when they need them. The package does not offer handouts; it empowers people to save for their future. The package contains many proposals -- both new and old -- that address three fundamental problems: portability, coverage, and security (enforcement).

1. PORTABILITY

The Portability Problem: Workers changing jobs currently face an obstacle course of barriers to consolidating their retirement accounts and continuing to save. Take the example of workers who are lucky enough to have a 401(k) plan (about 20 million are), but then are laid off or get a new job. They face the following obstacle course that trips up all too many.

1. Does their former employer let employees take their savings with them? While most employers do, 20% of employees covered by a 401(k) plan cannot.
2. If they cannot take their savings with them, they may lose investment options and will have to keep track of their savings and former employer -- sometimes over decades and thousands of miles.
3. Even if their former employer lets them take their savings with them, will their new employer accept 401(k) "rollovers"? Only half of participants are in plans that do.

4. Even if their new employer accepts rollovers, over three-quarters of 401(k) plans bar rollovers immediately upon hiring, usually requiring new employees to wait a year.
5. If their new employer does not let new employees rollover their old 401(k) savings account, they can either transfer the savings to an IRA or "cashout."
6. Transferring savings to an IRA requires workers to tip toe their way through tax and timing issues that many find difficult to navigate.
7. Those who successfully navigate the obstacle course, may have to keep separate IRA accounts for each former 401(k) plan -- and pay a management fee on each one.
8. Those who do not navigate it quickly enough are forced to cash out and pay a 20% tax.
9. Given this obstacle course, others who are struggling to get by may find the temptation to cashout irresistible, leaving them with inadequate savings for retirement.

Portability Proposals: The main new proposals in your pension package are the portability proposals to cut through this and other obstacle courses. Combined with the Kassebaum-Kennedy health insurance reforms, they would make it simpler for Americans changing jobs and provide more security, making it easier to take advantage of new possibilities in our changing economy. *Over 5 million workers* with pensions who change or lose their jobs each year could benefit from your pension portability proposals. Many provisions in the package would increase portability, including:

- **Eliminating barriers to workers' taking their 401(k) savings with them when they change jobs and to immediately start saving with the new employer.** It eliminates the legal barriers that discourage employers from letting employees transfer their retirement savings and immediately start contributing to a retirement plan. Currently, over three-quarters of all 401(k) plans bar new employees from immediately joining and transferring their 401(k) savings.
- **Enabling more workers to contribute to IRAs, including those whose new employer does not have a pension plan.** Your IRA proposal will enable *33 million* more Americans to contribute to an IRA. [Note that it is 33 million *Americans*, not workers, because more non-working spouses could contribute although they would still be subject to the current \$250 limit on contributions].
- **Reducing the time it takes for certain workers to be vested in their pension plan.** It reduces from 10 years to 5 the time it takes to be vested in a multiemployer plan (these are usually union plans covering workers who frequently switch employers such as construction workers).
- **Eliminating barriers to veterans -- usually reservists -- continuing in their pension plans after their service.**
- **Ensuring that workers receive the benefits to which they are entitled -- even if they have long since left that employer or the employer is no longer in business.**

Talking Points: *Workers currently face an obstacle course when they change or lose their job and want to take their retirement savings with them. This obstacle course is not a big problem for those who can afford an accountant, but it can trip up the average American. No wonder millions of Americans are anxious about their retirement savings in this time of economic change. This new proposal could make it easier for more than 5 million workers a year to take their retirement savings with them and continue to save when they change or lose their job.*

2. COVERAGE

The Coverage Problem: Only about 50% of full-time workers are covered by an employer-sponsored retirement savings plan (and far fewer part-time workers). Even fewer workers are covered by small businesses: only 24% of full-time workers in small businesses with fewer than 100 employees were covered in 1993, while 73% of full-time workers in firms with 1,000 or more employees were covered. Many workers have neither an employer-provided plan or an IRA.

Coverage Proposals: Your pension package contains your current proposals to expand coverage in both employer-provided plans and individual IRAs, including:

- **Creating a Small Business 401(k) Plan.** Your NEST proposal replaces the complexity that discourages many small businesses from offering pension plans:
 - Has no red tape: no complicated employer filing, testing, forms or calculations.
 - Allows workers to make deductible contributions of up to \$5,000 a year.
 - Employers could contribute 3% of an employee's pay or 1% of pay plus a matching formula.
 - All contributions would be fully portable and immediately fully vested.

Note: Senator Dole proposed a similar plan in December that would let employers cover themselves but not all their workers. Not surprisingly, his proposal has a strong appeal to many small businesses. But it is right for employers to provide their employees with the same security and opportunity to save that they provide their families. *[Is this the right line of defense, in light of corporate citizenship?]*

- **Making it easier for all employers to provide their employees with pension plans.** It will expand pension coverage at big and small firms by vastly simplifying complex pension rules and eliminating many unnecessary rules, tests, and reports.
- **Eliminating barriers to pension coverage for workers in their first year in a job.** It repeals the current laws that discourage employers from providing new employees with pensions for a year. Currently, over three-quarters of all 401(k) plans bar new employees from immediately participating in the plan.
- **Enabling 33 million more Americans eligible for deductible IRAs.**

- **Making IRAs -- and saving -- more attractive by allowing tax-free withdrawals for certain purposes.** Many people are reluctant to put their money in an IRA because they may need it if they lose their job and can't find a new one, to pay for education, their first home, or to cover unexpected medical expenses. The proposal allows penalty free withdrawals for these purposes.
- **Enabling non-profit organizations, such as the Boy Scouts and the Red Cross [check], to provide 401(k) plans.**

Talking Points: *Currently roughly 50 million Americans do not have an employer-provided pension plan -- over half of whom (28 million) work for a small business with less than 100 employees. Many do not have an IRA either -- and they worry what they will do when they retire and that they will be a burden to their children. These proposals will expand pension coverage by making it easier for every business to offer employees a pension plan and making 33 more Americans eligible for IRAs. Simplifying pension rules means more money will be saved for retirees and less will be spent on accountants, lawyers, actuaries, and consultants.*

3. SECURITY/ENFORCEMENT

The Security Problem: Workers should not have to worry that the money they have saved for retirement will be there when they retire. However, during the 1980s corporations siphoned off over \$20 billion from workers pension plans for corporate mergers, acquisitions, leveraged buyouts, and expenses. *And under the guise of reducing corporate subsidies, the Republican reconciliation bill would have given corporations the green light to do it again* and reduce pension funds assets by \$15 billion, affecting over 5,000 firms with 3.7 million workers. In addition, the Labor Department has found that a few employers misusing pension contributions or delaying investing contributions. Some 22 million people are now covered by 401(k) plans.

The Security Proposals: This package builds on our many accomplishments in this area, and addresses both employer misuse of pension contributions and pension reversions. It contains your legislative proposal to detect and promptly address the misuse of pension funds, and a new pension reversion proposal that combined will send a strong signal that we will continue to protect workers' savings. The package would:

- **Require prompt reporting and action on the misuse of pension funds.** The package significantly enhances the security of money in pensions funds by requiring accountants to promptly report delays in contribution transfers or misuse of funds. If the employer does not quickly respond to the problem, the accountants would have to report the problem directly to the Labor Department.

- **Protect workers' pensions from corporate raids.** The package will contain a proposal to protect workers pensions from being raided, although the content of proposal has still not been finalized. While Republicans want to make it easier for corporations to raid pension funds again, your new proposal will demonstrate your determination to protect workers' retirement savings. Specifically, the Republican proposal would have allowed corporations to divert pension funds without paying a tax. This penalty tax has successfully discouraged pension reversions since it was adopted in 1990.

Talking Points: *I am proud of what this Administration has already accomplished to secure the pensions of millions of Americans. Our 1994 law protects the benefits of more than 40 million workers. Secretary Reich is leading a nationwide effort to protect workers' 401(k) contributions, and has already returned over \$7 million to workers. This package contains a proposal to require the prompt reporting and action on pension fund misuse and a new pension reversion proposal that combined will send a strong signal that we will continue to protect workers' savings to ensure that it is there when they need it.*

This proposal is in sharp contrast to the proposal in the Republican budget that -- under the guise of reducing corporate subsidies -- would have once again given corporations the green light to reduce the pension funds assets of millions of workers by \$15 billion.



Pension Benefit Guaranty Corporation
1200 K Street, N.W., Washington, D.C. 20005-4026
(202) 326-4010

Office of the Executive Director

March 27, 1996

**TO: Ellen Seidman
Gene Sperling
Olena Berg
Mark Iwry**

SUBJECT: Pension Reversion Legislation

Memo on reversions with options. Thought you might want to look at it before we meet.

Attachment

~~CONFIDENTIAL~~
REVERSION LEGISLATION

DETERMINED TO BE AN
ADMINISTRATIVE MARKING
INITIALS: JAM DATE: 11/14/77
2016-0531-F

BACKGROUND

In the 1995 Budget Reconciliation Bill, Congress proposed that employers could remove certain so-called "surplus" funds from pensions. In vetoing the Bill, the President said: "People who work hard and save for retirement ought to be able to retire with dignity ... This bill would give companies the green light to raid pension funds and put those retirements at risk..."

1980's. During the 1980's, when pension assets grew with the stock market, companies tapped into the pension funds set aside tax-free for their employees' retirement. Companies took away more than \$20 billion from over 2,000 pension plans covering nearly 2.5 million workers and retirees.

It has been reported that pension funds were used in two-thirds of the largest buyout transactions in the 1980's. The Tengelmann Group used \$270 million in pension money to finance its takeover of A&P. The takeover was followed by a large downsizing and the end of A&P's longstanding practice of giving retirees cost-of-living increases in their benefits.

The spate of pension "reversions" resulted in immediate difficulties for some pensioners. The Pacific Lumber Company, a family-owned forest products company located in Northern California with a well-funded pension plan, was taken over in a leveraged buyout by the Maxxam Group. After the takeover, Maxxam terminated its pension and took over \$50 million to pay off debt associated with the buyout. Maxxam purchased annuities for workers in its terminated plan from the Executive Life Insurance Company, which later failed leaving Pacific Lumber workers facing reduced annuities.

In many cases, companies took money from an "overfunded" plan while allowing significant underfunding in another plan. Each year, PBGC issues a list of the 50 companies with the largest pension underfunding. Twenty companies on the list for at least one year since 1989 took large amounts from an overfunded plan. For example, the Goodyear Tire and Rubber Company, took a \$400 million reversion in 1988 from its plan for salaried workers. Goodyear's pension plan for tire and rubber workers is now underfunded by \$93 million.¹

In some cases, the same plans from which a reversion was taken are now significantly underfunded. The Enron Corporation, a Houston oil and gas company, removed \$232 million from its pension plan in 1986. The plan was most recently reported to be underfunded by \$27 million. ASI Holding Corporation, an air conditioning,

¹In February of this year, Birdsboro Corporation, a Pennsylvania steelmaker with 595 people, terminated its plan for steelworkers with about \$3.8 million underfunding. Birdsboro took a \$4.4 million reversion from its plan for executives and white collar workers in 1986.

~~CONFIDENTIAL~~

plumbing and automotive products company headquartered in New Jersey employing 37,800 workers, took \$120 million from a plan now underfunded by \$72 million.

Congressional Response. In 1990 Congress acted to stem the tide of pension reversions. Companies who terminated pension plans had to pay a 50% excise tax on any surplus remaining when a plan terminates, or 20% if the company replaces a pension plan with a new plan. Companies were able to withdraw assets from ongoing plans on a limited basis strictly for retiree health expenses.

1995 LEGISLATION.

The House voted to allow employers to take almost freely massive amounts from ongoing pensions, without notice to workers. Even though the Senate voted against withdrawals, the Congressional Conference Committee developed a proposal that would allow companies to take money from pensions that are more than 125 percent funded on a PBGC termination basis. There would be no excise tax and again no notice.

Some 6,000 pension plans, covering nearly 4 million workers and retirees, have about \$24 billion in assets subject to withdrawal. It was projected that \$15 to \$18 billion would be removed from pensions over the next five years.

As the legislation was working its way through, Administration officials pointed to the risk that it posed to pensions and the pension insurance system.

- ◆ A plan that is overfunded can quickly become underfunded with a change in interest rates and asset values. A reduction in the interest rate of 2 percentage points can reduce the funding level from 125% to 92%.
- ◆ Pension plans subjected to reversions in the past have become underfunded over time.
- ◆ The proposal reduces the national savings rate by allowing long-term retirement savings pay for current expenses.
- ◆ The proposal reduces savings at the very time that the "Baby Boomers" are nearing retirement age. We should be increasing, not depleting, savings to meet their retirement needs. There are 80 million baby boomers (born 1946-1964) who will retire in the future.
- ◆ The proposal allows employers to use tax-subsidized pension funds for non-retirement purposes. It opens the door to tax gaming by allowing pension reversions to be timed to a tax loss year.

ADMINISTRATION PROPOSAL.

Option 1: No Reversions to Employers

As a practical matter, reversions have slowed to a trickle since the stiff excess tax

was imposed in 1990. Still, to close the issue and stake out our ground clearly, we could propose legislation that would put an end to reversions of pension funds to employers.

This proposal would prohibit reversions from qualified defined benefit pension plans. Any reversion from such a plan would violate ERISA. On plan termination, employers would have to transfer excess assets to employees as increased benefits or to another plan.

Option 2: Notice to Workers

Current law requires a company to notify workers that a plan is going to terminate 60 days before the expected date of termination. Employees need not be told whether their employer expects to get back plan moneys.

We could propose legislation that would require employers to tell employees, as part of the termination notice, whether there are surplus assets and the amount expected to go back to the employer.

Discussion

Prohibiting reversions is a stronger proposal. This legislation would keep pensions safe, making sure that money grows in people's pensions and that benefits are there when needed. The President would challenge the Congress to make sure once and for all that hard-earned benefits are preserved.

The proposal does carry risks. We have had the support from legislators of both parties on pension issues. Employer groups will vigorously oppose this provision. They will argue that prohibiting reversions discourages defined benefit plans and stronger funding of such plans. Also, because they must make up any shortfall, employers feel they should be able to recover any excess. Opposition could divert attention and reduce support for other parts of the pension package.

A notice provision would bring what reversion activity there is to light. As we have learned from the Retirement Protection Act, notices have an appeal; they provide information to workers and incentives for employers. It is unlikely that business opposition could gather momentum, particularly since employers already must give the notice of intent to terminate to workers and will have already estimated the reversion amount as part of the decision to terminate the plan.

A notice proposal however is more moderate. It leaves the impression that a lot of reversion activity is going on, and that the Government is countenancing it. It gives the President an opportunity to remind Americans that the Administration protected their pensions and that it will continue to be the guardian of their benefits, but it does not carry the clear message an outright ban on pension takings would carry.²

²A notice requirement could be effected by regulation.

TOP 50 POST-1985 REVERSIONS

ANK	SPONSOR	DATE	ASSETS (IN MILLIONS)	REVERSION (IN MILLIONS)
1	EXXON CORP.	12-Aug-86	\$5,200	\$1,600
2	GOODYEAR TIRE	30-Jun-88	\$930	\$400
3	PHILLIPS PETROLEUM	01-Sep-86	\$1,090	\$400
4	MERRILL LYNCH	13-Dec-88	\$1,012	\$243
5	ENRON	30-Jun-86	\$254	\$232
6	ASHLAND OIL INC	02-Jan-87	\$386	\$165
7	N L INDUSTRIES	01-May-86	\$300	\$150
8	AMER. NAT. RED CROSS	31-May-89	\$386	\$128
9	DRESSER INDUSTRIES	30-Apr-86	\$580	\$124
10	RELIANCE ELECTRIC	01-Jul-87	\$280	\$120
11	AMERICAN STANDARD	30-Jun-88	\$625	\$120
12	TRANSCO	01-Mar-86	\$187	\$115
13	SHERWIN - WILLIAMS S	01-Aug-86	\$309	\$107
14	PS GROUP	30-Jun-88	\$110	\$106
15	OCCIDENTAL PETROLEUM	15-Mar-88	\$382	\$96
16	MORRISON KNUDSEN	12-Dec-87	\$127	\$82
17	PENNZOIL	30-Aug-86	\$289	\$71
18	PERALTA HOSPITAL	31-Dec-88	\$69	\$67
19	CABOT CORP	15-May-88	\$61	\$60
20	BAKER INTERNATIONAL	09-Jun-86	\$173	\$56
21	C B I INDUSTRIES	31-Dec-87	\$91	\$55
22	AMAX-SALARIED	30-Apr-87	\$135	\$54
23	TRIANGLE PUBLICATION	15-Feb-89	\$115	\$50
24	PACIFIC LUMBER	31-Mar-86	\$80	\$50
25	ST. VINCENT MEDICAL	31-Mar-89	\$86	\$49
26	ASAR CO.	30-Jun-87	\$189	\$49
27	EMERY AIR FREIGHT	31-Oct-87	\$59	\$49
28	JOY TECHNOLOGIES	25-Sep-87	\$107	\$47
29	1ST NAT.BANCORP OF T	31-May-87	\$65	\$44
30	DESOTO SALARIED	31-Dec-90	\$80	\$43
31	STANADYNE-SALARIED	02-Jul-88	\$102	\$41
32	JOHNSON CONTROLS	01-Dec-90	\$107	\$41
33	BABCOCK & WILCOX	31-Dec-89	\$154	\$41
34	AMINOIL	30-Jun-88	\$77	\$41
35	GUY F. ATKINSON CO.	01-Dec-87	\$69	\$40
36	BECOR WESTERN	01-Sep-86	\$115	\$40
37	AMCA INT'L	30-Jun-87	\$116	\$39
38	AMSTAR	30-Jun-87	\$84	\$39
39	FIGGIE	21-Nov-88	\$121	\$37
40	FISCHBACH	30-Nov-88	\$90	\$35
41	INTERLAKE CO's	31-Dec-86	\$49	\$32
42	BLUE CROSS - CA.	10-Dec-86	\$95	\$32
43	GATES LEARJET	31-Jan-86	\$55	\$30
44	ASHLAND OIL INC. SAL	02-Jan-87	\$74	\$30
45	NEW ORLEANS PUB.SERV	01-Oct-88	\$123	\$30
46	KELSEY-HAYES	31-Dec-86	\$109	\$29
47	PRESBYTERIAN HOSPITA	31-Dec-87	\$31	\$29
48	PIONEER	10-Dec-86	\$69	\$29
49	DOUBLE DAY & CO	31-Dec-86	\$92	\$28
50	PRIMARK	01-Sep-88	\$29	\$27

**Companies Appearing on at Least One Top 50 List That Took a Reversion
From One or More of Their Plans (Dollars in Millions)**

<u>Company Name</u>	<u>1995 - Vested Underfunding</u>	<u>Amount of Reversion(s)</u>	<u>Date of Reversion(s)</u>
Anchor Glass Container Corp.	\$126.30	\$4.75	7/31/85
ASI Holding	\$72.00	\$119.90	6/30/88
Bethlehem Steel	\$1,573.00	\$1.40	12/31/82
Budd Co.	\$122.80	\$1.30	8/6/85
Cooper Industries	\$47.80	\$20.92	7/18/83, 6/30/88
Del Monte Foods	\$67.90	\$12.34	6/30/88
First Finl. Mgt. (Western Union)	\$179.30	\$16.20	11/15/88
Goodyear Tire & Rubber	\$92.80	\$400.00	6/30/88
Harnischfeger	\$11.50	\$38.01	8/1/84
Libbey-Owens-Ford	\$77.50	\$52.02	10/6/85
Lone Star Technologies	\$44.30	\$54.27	11/30/85
LTV Corp.	\$1,558.70	\$2.09	5/1/85
Maxxam	N/A	\$50.00	3/31/86
Occidental Petroleum	\$53.20	\$181.90	6/1/83, 3/15/88
Reynolds Metals	\$98.40	\$126.00	8/22/83
RJR Nabisco	\$6.40	\$2.00	6/30/88
Tenneco	N/A	\$1.00	8/15/87
Continental Airlines	\$128.20	\$2.14	1/31/82
UAL Corp.	\$407.10	\$378.15	7/5/85
Uniroyal*	\$362.00	\$4.00	9/10/87
Chiquita Brands (United Brands)	\$79.70	\$15.20	5/1/85
Variety Corp.	\$4.90	\$29.00	12/31/86

Underfunding calculated as of 12/31/94

* Underfunding relates to Uniroyal-Goodrich Tire - reversion was taken by its predecessor - Uniroyal Inc.

1995 OVERFUNDED PLANS

(DOLLARS IN MILLIONS)

OVERFUNDING	\$231,530
ASSETS	\$917,961
LIABILITIES	\$686,431
PARTICIPANTS	23,966,497
PLANS	11,870

Estimates based on 1993 Form 5500 filings for plans with 100 or more participants.

Liabilities were adjusted to 5.60% interest rate and GAM-83 mortality.

Assets were adjusted by 21.39% to reflect extraordinary financial market activity in 1995.

Actual values may vary from these estimates.

TOP 100 OVERFUNDED PLANS

(DOLLARS IN MILLIONS)

<u>RANK</u>	<u>SPONSOR</u>	<u>EIN/PIN</u>	<u>OVERFUNDING</u>	<u>PARTICIPANTS</u>
1	GENERAL ELECTRIC COMPANY	140689340001	\$8,230	455,640
2	AT&T CORP	134924710005	\$5,418	262,237
3	INTERNATIONAL BUSINESS MACHINES	130871985001	\$4,575	289,829
4	AT&T CORP	134924710006	\$4,187	180,491
5	AMERITECH CORPORATION	363251481002	\$3,066	80,873
6	BELLSOUTH CORPORATION	581533433005	\$2,956	91,797
7	PRUDENTIAL INS CO OF AMERICA	221211670003	\$2,869	74,824
8	FORD MOTOR CO	380549190002	\$2,794	108,874
9	U S WEST INC	840926774005	\$2,793	109,264
10	AMERITECH CORPORATION	363251481001	\$2,565	42,788
11	PACIFIC TELESIS GRP	942919931002	\$2,300	69,846
12	STATE FARM MUTUAL AUTO INS	370533100001	\$2,253	74,364
13	BELLSOUTH CORPORATION	581533433006	\$2,225	43,669
14	NORTHROP CORP	951055798010	\$2,045	49,733
15	GTE SERVICE CORPORATION	131675522002	\$1,921	26,653
16	PACIFIC TELESIS GROUP	942919931001	\$1,920	38,369
17	NYNEX CORPORATION	133180909012	\$1,856	98,305
18	NYNEX CORPORATION	133180909013	\$1,849	49,365
19	SOUTHWESTERN BELL CORP	431301883006	\$1,773	95,274
20	BOEING CO & CONSOLIDATED	910425694001	\$1,702	200,625
21	BELL ATLANTIC CORPORATION	232259884002	\$1,657	79,820
22	MCDONNELL DOUGLAS CORP	430400674001	\$1,643	73,810
23	LOCKHEED CORPORATION	950941880001	\$1,624	79,097
24	GTE PRODUCTS OF CONNECTICUT	132884758001	\$1,565	5,289
25	KRAFT GENERAL FOODS INC	363083135150	\$1,464	82,329
26	PACIFIC GAS & ELECTRIC CO	940742640001	\$1,414	42,346
27	HUGHES AIRCRAFT COMPANY	951778500001	\$1,377	71,721
28	ROCKWELL INTERNATIONAL	951054708001	\$1,230	69,351
29	GENERAL DYNAMICS CORP	131673581001	\$1,094	53,809
30	GTE CALIFORNIA INC	950510200001	\$1,094	17,750
31	FLORIDA POWER & LIGHT COMPANY	590247775001	\$1,033	18,265
32	DOW CHEMICAL CO	381285128001	\$967	42,930
33	BELL ATLANTIC CORPORATION	232259884001	\$949	37,430
34	CITIBANK N A	135266470001	\$945	75,321
35	CONSOLIDATED EDISON CO OF N Y	135009340001	\$945	22,894
36	SHELL PENSION TRUST	746171856001	\$944	48,132
37	NATIONAL RURAL ELECTRIC COOP	530116145333	\$941	51,041
38	GOODYEAR TIRE & RUBBER CO	340253240002	\$906	25,934
39	CHEVRON CORPORATION	940890210006	\$875	66,697
40	GEORGIA POWER COMPANY	580257110001	\$863	18,009
41	USX CORPORATION	250996816001	\$857	148,985
42	DIGITAL EQUIPMENT CORP	422265900001	\$855	67,216
43	DELTA AIR LINES INC	580218548002	\$813	69,769
44	SOUTHERN CALIFORNIA EDISON	951240335001	\$808	25,366
45	SPRINT CORPORATION	480457967001	\$726	65,538
46	INTERNATIONAL PAPER COMPANY	130872805105	\$720	26,794
47	MARTIN MARIETTA ENERGY SYSTEMS	521318516001	\$695	22,559
48	MOBIL OIL CORP	135401570001	\$677	46,571
49	SANDIA CORP	850097942006	\$662	10,048
50	CHEMICAL BANK	134994650001	\$653	45,990
51	METROPOLITAN LIFE INSURANCE	135581829001	\$645	39,226
52	ALABAMA POWER COMPANY	630004250001	\$608	12,172
53	TENNECO INC	760233548300	\$592	62,839
54	GTE SERVICE CORPORATION	131675522001	\$580	21,366
55	MARATHON OIL CO	251410539001	\$576	11,969

TOP 100 OVERFUNDED PLANS

(DOLLARS IN MILLIONS)

<u>RANK</u>	<u>SPONSOR</u>	<u>EIN/PIN</u>	<u>OVERFUNDING</u>	<u>PARTICIPANTS</u>
56	PENNSYLVANIA POWER & LIGHT	230959590001	\$572	10,763
57	CONSOLIDATED RAIL CORP	231989084001	\$568	18,961
58	CATERPILLAR INC	370602744002	\$560	28,482
59	ELI LILLY & CO	350470950001	\$558	23,607
60	NCR CORPORATION	310387920001	\$553	42,485
61	TRW INC	340575430007	\$552	81,671
62	FEDERAL EXPRESS CORP	710427007002	\$534	79,023
63	SAFEWAY INC	943019135001	\$531	19,654
64	MONSANTO CO	430420020001	\$529	36,036
65	ARMSTRONG WORLD INDUSTRIES	230366390001	\$528	21,185
66	NORTHERN STATES POWER CO	410448030001	\$519	11,811
67	SEARS ROEBUCK & COMPANY	361750680002	\$507	242,007
68	FIRST NATIONAL BANK OF CHICAGO	360899825002	\$504	15,779
69	ATLANTIC RICHFIELD COMPANY	230371610091	\$497	50,460
70	DELTA AIR LINES INC	580218548005	\$494	10,280
71	TEXTRON INC	50315468076	\$482	35,945
72	J C PENNEY COMPANY INC	135583779001	\$474	157,897
73	ABBOTT LABORATORIES	360698440001	\$471	38,148
74	UNITED TECHNOLOGIES CORP	60570975001	\$467	112,694
75	NORTHEAST UTILITIES SERVICE	60810627001	\$467	16,807
76	NATIONWIDE MUTUAL INSURANCE	314177100001	\$466	30,012
77	ANHEUSER-BUSCH COMPANIES INC	431162835003	\$462	18,274
78	DIRECTORS OF FINANCIAL INSTS	135645888333	\$460	35,790
79	PFIZER INC	135315170001	\$451	23,741
80	TIMES MIRROR COMPANY	951298980001	\$443	28,603
81	RAYTHEON CO	41760395001	\$439	38,278
82	CHEMICAL BANK	134994650005	\$439	226
83	UNION OIL CO OF CALIFORNIA	951315450001	\$439	19,224
84	MELLON BANK N A	250659306001	\$439	23,153
85	R R DONNELLEY & SONS CO	361004130001	\$438	34,759
86	CHEMICAL BANK	134994650006	\$437	20,319
87	JOHNSON & JOHNSON	221024240001	\$430	47,726
88	CONSOLIDATED EDISON CO OF N Y	135009340005	\$425	10,232
89	SOUTHERN CALIFORNIA GAS CO	951240705001	\$423	14,983
90	NYS ELECTRIC & GAS CORP	150398550001	\$420	7,181
91	AMOCO CORPORATION	361812780002	\$419	52,799
92	TELEDYNE INC	952282626100	\$418	24,309
93	GTE PRODUCTS OF CONNECTICUT	132884758036	\$417	15,947
94	KAISER PERMANENTE MED CARE	946365467001	\$412	49,669
95	NEW YORK LIFE INSURANCE	135582869001	\$411	7,920
96	JOHN HANCOCK MUTUAL LIFE INS	41414660001	\$410	23,440
97	MARTIN MARIETTA TECHNOLOGIES	520740018001	\$406	42,430
98	GTE FLORIDA INCORPORATED	590397520001	\$406	8,799
99	BROWN & WILLIAMSON TOBACCO	610144470001	\$404	6,300
100	SOUTHERN NEW ENGLAND TELEPHONE	60542646005	\$401	12,306

Estimates based on 1993 Form 5500 filings for plans with 100 or more participants.

Liabilities were adjusted to 5.60% interest rate and GAM-83 mortality.

Assets were adjusted by 21.39% to reflect extraordinary financial market activity in 1995.

Actual values may vary from these estimates.

**UNITED STATES DEPARTMENT OF LABOR****FACSIMILE TRANSMISSION****OFFICE OF CONGRESSIONAL AND INTERGOVERNMENTAL AFFAIRS**

200 Constitution Avenue,
N.W.
Room S-1325
Washington, DC 20210

Confirmation:
202/219-6141

June 7, 1994/4:47pm

TO: GENE SPERLING

DEPARTMENT/COMPANY: OFFICE OF ECONOMIC POLICY

FACSIMILE NUMBER: 456-2878

FROM: DARLA LETOURNEAU

NUMBER OF PAGES INCLUDING COVER: 3

FACSIMILE REPLIES:

CONGRESSIONAL AFFAIRS

202/219-5120

INTERGOVERNMENTAL AFFAIRS

202/219-5736

IMMEDIATE OFFICE OF THE ASSISTANT SECRETARY

202/219-5288

MESSAGE: *Per Kitty Higgins' conversation with you yesterday, attached is a note I did for the Secretary yesterday on the Crime Trust Fund issue. Please call me if you have any questions - 219-6141.*

6/6/94

NOTE TO: SECRETARY REICH

FROM: DARLA LETOURNEAU 

RE: CRIME TRUST FUND ISSUES

The Administration is nearing completion of its letter to the conferees on the crime bill, which will include draft legislative language to make modifications to the Trust Fund proposal. As part of this process and the subsequent congressional deliberations in conference, several decisions will be made that will directly or indirectly impact on the President's Investment Package. It is important that the White House be fully aware of these impacts and factor them into their deliberations.

This memo ultimately recommends that DOL weigh in on one such issue now--the treatment of the Exon-Grassley cut--both because of its direct impact on the President's Investment Package and as a step towards flagging this general issue for the Administration's attention.

For FY 1995, OMB is working to try to ensure that the funds to establish the Trust Fund only come from the State/Commerce/Justice subcommittee's allocation, since the President's budget request included the \$2.4 billion necessary to fully fund the first year of the crime bill. They are hopeful that the C/J subcommittee will reserve the \$2.4 billion plug number until after the conference completes work. We will know after the C/J subcommittee's mark-up on Wednesday whether that plan has been adopted.

At that point, the Administration is planning to submit an FY 1995 budget amendment that reflects a modified proposal for how to spend the \$2.4 billion, reflecting some new crime programs (such as YES) that were not included in the President's initial budget request. Through this process, the Administration would be signaling that they want some of the funds to be allocated to other subcommittees, such as L/HHS or VA/HUD, for prevention activities.

Although the Administration can signal its priorities, as it does with the President's annual budget request, the Appropriations Committees will ultimately decide from which subcommittee(s) to take the funds to create the Trust Fund and which subcommittee(s) should receive an allocation from that Trust Fund. The individual subcommittees will then decide which programs authorized in the crime bill will receive those funds.

In the outyears, the discretionary caps will simply be lowered by the amount of the crime bill--proposed to be \$4.3 billion in BA and \$2.3 billion in outlays in FY 1996 (and \$6.5 billion in FY 99). In total, the reduction is likely to be \$23-28 billion over 5 or 6 years. The Administration's position is that the full cost of the crime bill was included in the President's FY 1995 Budget five-year

numbers; therefore, spending for these programs was already assumed.

However, since the President's budget was submitted, the Congress adopted the Exon-Grassley amendment as part of the FY 1995 Budget Resolution, which results in a reduction of \$30.8 billion BA and \$13 billion in outlays over the same five year period.

The President's Investment Package includes an increase of \$13.7 billion in discretionary spending (BA) in FY 1995 (compared to FY 1994). Between FY 1995-99, the spending on investments are slated to increase by approximately \$19.5 billion in BA (and \$31.1 billion in outlays).

The size of the President's Investment Package is roughly comparable in size to the crime bill in terms of funds to be spent over the next 5 years. Although the President started the FY 1995 budget process with sufficient funds to fully fund the crime bill, the impact of the Exon-Grassley cut now complicates the picture. As currently constructed, the Crime Trust Fund is protected from the Exon-Grassley cut and will be funded at 100 percent. Thus, the shortfall in funding will come from the remaining discretionary spending accounts. If defense is protected from these cuts, then the full brunt will fall on the domestic discretionary accounts and within those, primarily on the President's Investment Package.

Given the downward pressure on the discretionary spending, it is essential that the Administration carefully consider the impact of the design of the Crime Trust Fund on the President's Investment Package. The Administration should consider whether, given the reduction in the spending caps since the Senate adopted the Crime Trust Fund provision, the Trust Fund should be reduced to reflect its share of the Exon-Grassley cut.

If that is not feasible at this point, then the Administration should consider proposing language in the Trust Fund provisions that would make it clear that if Congress adopts future reductions in the spending caps, the Crime Trust Fund would not be exempted from this process. Given the fact that the Congress has reduced the spending caps below the 1990 Budget Enforcement Act agreement in each of the last two years, there is no reason to believe that we will not face yet more reductions in these caps in future years during the life of this Crime Trust Fund.

Recommendation: I recommend that we take steps to raise this issue within Administration circles so that throughout the remaining deliberations on the Crime Trust Fund, its impact on the President's Investment Package is taken into account. As a first step, I would recommend discussions with Gene Sperling. At a minimum, we should propose that the Trust Fund not be exempted from any future reductions in the discretionary spending caps.

U.S. Department of Labor

Chief of Staff to the
Secretary of Labor
Washington, D.C. 20210



MAR 30 1994

MEMORANDUM FOR: GEORGE STEPHANOPOULOS
GENE SPERLING
MARK GEARAN

FROM: KITTY HIGGINS *Kitty*
DOUG ROSS *D.R.*
ANNE LEWIS *AL*

SUBJECT: Rhetoric on the "Unemployment System and
Political Fallout"

We need your help positioning the Reemployment Act so that the primary message -- we need a reemployment system -- does not become obscured by a secondary point which is both inaccurate and inflammatory -- the unemployment system we have is worthless.

Midway through his remarks at the G-7 Conference, the President said:

"it is wrong to charge employers an unemployment tax, to put it in a trust fund to pay people when they are unemployed to hang around until the unemployment runs out when they still won't have a job. That is not right."

Unfortunately, this was not the first time UI has been mis-characterized. In a November, 1993 speech delivered to the Asian Pacific Economic Council, the President described the "unemployment" system as an "unfair tax on employers because it doesn't function, and a rip-off for employees because it doesn't help them".

Such sweeping condemnations of the entire UI system have raised great concern on Capitol Hill and among organized labor. (A letter from Lane Kirland to the President, and a memo from Rick McGahey with the Joint Economic Committee, are attached as illustrations.) They irritate our allies, and also mis-characterize the problem we're addressing and the remedies we propose.

We need to be clear about what is broken. The facts are that the UI system is quite successful at the task for which it was originally designed -- paying short-term income to temporarily laid-off workers. Although large numbers of workers change jobs on their own and collect UI for a short time, the problem is that the system's mission fails to meet the most common need of many other jobless workers today. Most unemployed workers now face permanent unemployment, and by the time workers exhaust their UI benefits, only 6 percent will have attended job search assistance activities, and only 1.4 percent will have received any kind of training. UI is a well-functioning, but partial, component of a system that is, in total, inadequate to modern needs.

What's broken is the patchwork of job training and reemployment programs narrowly targeted on various causes of dislocation. These are fragmented, not coordinated and have varying eligibility requirements, services, and benefits. There's little accountability and training is often provided without regard to outcomes. Customers have few choices of service providers.

The UI system pays about eight and one half million people a year -- many on temporary lay-off who do get recalled to their old jobs. About 25 percent are dislocated workers. The system needs adjustment to focus on early intervention for those UI claimants -- only about a third of the total -- who are in danger of exhausting benefits before finding another job. We're implementing a system of "profiling", or early identification, to pinpoint workers in need of reemployment assistance. The Reemployment Act also refines UI by extending longer-term benefits through the UI system to the emerging customer base of workers who need retraining to find new jobs.

We believe that in discussing changes an accurate portrayal of what is broken is important to avoid major misunderstandings or political backlash. The "welfare cheat" analogies are not appropriate for millions of Americans with strong work histories, who are out of work through no fault of their own, and who look for work every week.

We need your help to ensure a more positive tone and focus on our proposal to build a new reemployment system.

Attachments

March 22, 1994

TO: Tom Glynn

FROM: Rick McGahey

SUBJECT: Characterizations of unemployment insurance by
President and Secretary

I had called you last week to alert you that key staff and members were upset by the way that the President and the Secretary have been characterizing unemployment insurance, as part of their argument in favor of the reemployment legislation. As the attached letter will show, it's now manifested in a letter from the AFL-CIO to the President and Bob. (I'm sending you this fax because I wanted to alert you to this, and because we've had trouble hooking up on the phone.)

One of the arguments for the reemployment act is that people used to go back to their old job, so unemployment served to tide them over until they went to work again with the same employer. But now, it is argued, people don't return, so it isn't fair to ask employers to pay taxes into the system. (The Secretary used this line of argument at the Metzenbaum hearing last week.)

This is factually incorrect. Most people on UI have never gone back to their previous job; the percentages now are even lower, but it is not correct to say that its a qualitative difference. The President then apparently ad-libbed in Detroit the line about "hang (ing) around until unemployment runs out," which prompted the Kirkland letter.

But more importantly, its not clear where this rhetoric takes you. Why undermine the social insurance basis for unemployment? If you tell employers it isn't "fair" for them to pay in, why is it any more "fair" for them to pay a surtax to reemploy dislocated workers?

Politically, employers aren't going to carry this legislation forward. It will be people who care about workers, unions, etc. There's no point in irritating them with this type of incorrect analysis and rhetoric; there are other ways to advance the argument for the reemployment bill. And the Administration shouldn't be undercutting the social insurance rationale for unemployment, especially when you hope to use the surtax funds to help pay for it.



815 Sixteenth Street, N.W.
Washington, D.C. 20006
(202) 637-6000

EXECUTIVE COUNCIL
LANE KIRKLAND PRESIDENT

Albert S. Eichen
Wayne C. Glenn
Vincent A. Smeraglio
Marion J. Woods
Lynn R. Williams
Gene Urshaw
Jack Shandman
Max Giller
Richard L. Thomas
Michael Barnes
Frank Hurl

THOMAS R. DONAHUE SECRETARY-TREASURER

Edward I. Harney
John J. Brennan
Gerald W. McElaine
Owen Seiber
Marion Daly
Jey Math
John J. Barry
George J. Kouroupas
Frank Hanley
Ron Carey
Linda Chavez-Thompson

William M. Wynn
James S. Hayfield
William H. Oyster
John T. Joyce
Robert A. George
Londie Moler
Squire Lucassen
John M. Rinderson
James J. Norton
Arthur A. Cole
Charles Johnson

March 18, 1994

The President
The White House
Washington, D.C. 20500

Dear Mr. President:

In your March 14 remarks at the Detroit G-7 meeting you said "... it is wrong to charge employers an unemployment tax, to put it in a trust fund to pay people when they are unemployed to hang around until the unemployment runs out when they still won't have a job. That is not right."

The UI system is far from perfect, but for millions of American workers it makes the difference between dignity and destitution. Some two-thirds of UI recipients get jobs before they exhaust their regular state UI benefits. Too often there are no jobs available for job-seekers with or without retraining.

The requirement that recipients show that they are actively seeking work, and not just "hanging around" until benefits run out, is actively enforced in every state system that I know of. Furthermore, the most glaring fault in the system is not that some may get it who shouldn't, but that far too many who should, don't -- because of employer-inspired restrictions and qualifications on eligibility, designed not to improve the system, but to limit access so as to hold employer taxes down.

The AFL-CIO will continue to work for improvements and reforms in the UI system, but we support the social insurance approach to income support for jobless workers.

Sincerely,

President

cc: Secretary Reich

TO:
Gene S

3pp total

Here is a rewritten memo with the decisions including retroactivity. I also clarified the language at the bottom of p. 1 that concerned Jack Quinn.

Let me know if you want me to talk to Damus prior to the meeting, or if you want me to set the meeting up. My view is that the principals' meeting should occur before we go to Damus to redraft the EO. As the compromises float through OMB, word could leak out before everyone is agreed, and the content might change in the principals' meeting anyway.

Also, I'm sorry to have brought it up again, but the \$100,000 threshold may be a serious problem for Labor. The draft EO applies that threshold only to termination, not to debarment, and Labor probably thinks the final version will stay that way. They may argue that the EO will be severely and unnecessarily blunted if the Secretary can do nothing to companies with only small contracts.

Separate FYI: I am compiling war on children info and should have something far better by tonight.

Thanks.



02/27/85 15:25 2102 400 2225

COMPROMISE PROVISIONS AND UNDERSTANDINGS PERMANENT STRIKER REPLACEMENT EXECUTIVE ORDER

The President and the Vice President have made decisions on three central issues concerning the executive order on permanent striker replacement. There are now three more technical issues that remain open. This document outlines the decisions already made and offers compromises on the outstanding issues. These compromises require both new language for the executive order and new understandings about how regulations will be developed and how the order will be applied. The explicit language and the understandings about the executive order are described below.

Decisions

1. Available Sanctions.

The Secretary of Labor could have authority only to terminate existing contracts, or also to debar contractors from obtaining new contracts. The Executive Order will give the Secretary both termination and debarment authority.

2. Dollar Threshold

The Executive Order could apply to companies with contracts of any size or only to companies with contracts in excess of \$100,000, the Simplified Acquisition Threshold. The Executive Order will apply only to companies with contracts above that amount.

3. Retroactivity

In the event that a company has permanently replaced strikers prior to the effective date of the Executive Order, the Secretary may not terminate that company's contracts, but the Secretary may debar the company from receiving future contracts.

Suggested Compromises

1. Period of Debarment

How long can a debarment last?

Provision

New Sec. 4(c): The period of the debarment may not extend beyond the date when the labor dispute precipitating the permanent replacement of lawfully striking workers has been resolved, as determined by the Secretary.

Understanding

In order to prevent permanent debarment, we have agreed that debarment will extend no longer than the precipitating labor dispute. However, the Secretary of Labor will have some discretion, so that in the event a strike ends and a union is broken while important aspects of the labor dispute persist, he will not have to declare the dispute "resolved." The Secretary will not delay declaring a strike resolved just so that a company can be punished after a dispute is resolved.

2. Scope of Debarment

How widely within a company can a debarment apply?

Provision

Rename Sec. 4 as Sec. 4(a) and add following as Sec. 4(b): The scope of the debarment will normally be limited to those Organizational Units, as defined by regulation, that the Secretary finds to have permanently replaced lawfully striking workers.

Understanding

The Secretary may apply debarments across product lines within a single company, even if the company has not replaced workers on all those lines (e.g., different kinds of sports gear within Nike). But the Secretary shall not apply debarments across entire conglomerates, where different companies in the conglomerate have little connection with or control over each other (e.g., food companies and tobacco companies in RJR/Nabisco). A firm that preserves good relations with its workers should not be penalized because it is owned by a holding company that also owns a firm that is permanently replacing strikers. But a firm that is permanently replacing workers on smaller product lines should not be able to avert debarment on bigger lines by not replacing only the workers on those lines.

3. Trigger for Debarment

In what circumstances can the Secretary investigate--and make a finding concerning--a company's practices?

Provision

Replaces first sentence of Sec 2. (a): The Secretary of Labor ("Secretary") may investigate any Federal Contractor, as defined by regulation, to determine whether that Contractor has permanently replaced lawfully striking workers.

Understanding

To the extent possible, "federal contractor" will be defined by regulation in keeping with the understanding under point 2, above. The Secretary will use whatever additional discretion is necessary to apply the provision in keeping with this understanding.

● Gene,

Came up with attached while
talking with Kelman.

OK by him.

● Will talk to Sam tonight; if
he's no go, ~~Don't~~ think

you might use this as basis
with Judge Mike tomorrow.

Robert

Suggested Compromise on Executive Order

1. Trigger for Debarment

Labor: Secretary may investigate any government contractor to determine whether the contractor has permanently replaced lawfully striking workers.

OFPP: Secretary may investigate any government contractor to determine whether the contractor has permanently replaced lawfully striking workers in the performance of a government contract.

Compromise: Secretary may investigate any government contractor to determine whether the contractor has permanently replaced lawfully striking workers producing the ~~same~~ product ~~as~~ supplied under the government contract.

2. Scope of Debarment

Labor: No limit on scope.

OFPP: The scope of the debarment will normally be limited to those organizational affiliates [a term of art] of the contractor that the Secretary of Labor finds have permanently replaced lawfully striking workers.

Compromise: The scope of the debarment will normally be limited to those entities [not a term of art] that the Secretary finds have permanently replaced lawfully striking workers. [I.e., Secretary can determine meaning of "entity."]

3. Period of Debarment

Labor: No limit on length.

OFPP: The period of debarment may be as long as three years, but ^{if} ~~not~~ no event may the period of debarment be longer than the period during which the contractor continues to employ permanent replacement workers as determined by the Secretary.

Compromise: The period of the debarment may be ^{no} longer than the period during which the contractor continues to employ permanent replacement workers as determined by the Secretary.

Revised

Gene,

RE: Striker Replacement EO

Please see attached. The descriptive part is just a shortened version of the Labor memo. The second and third parts are pros and cons. Concerns:

1. The memo may tilt too far against the EO. Perhaps argument (D) could be included in the discussion section, thereby keeping pros and cons to 3 each.
2. The "image" argument against the EO is included (i.e., "Old Democrat") in the cons, but the image argument for the EO is not included (i.e., appears strong and Presidential) in the pros. I thought it would be odd to put in a memo.
3. There is no discussion of the coverage threshold issue, which Labor only added in this latest iteration.
4. Elaine Kamarck is expecting to hear from you today.

Maybe you and I should sit down early tomorrow to review?

Robert

MEMORANDUM FOR THE PRESIDENT

FROM:

SUBJECT: STRIKER REPLACEMENT EXECUTIVE ORDER

The Labor Department has prepared a draft executive order (the "striker replacement EO" or "EO") that would prohibit employers that have permanently replaced striking union members from obtaining federal contracts and suspend the contracts of any employers who permanently replace strikers during the term of their federal contract. A dollar threshold could easily be added to the EO to limit the number of contractors covered. The draft executive order (tab 1) and a legal memorandum analyzing the EO (tab 2) are attached. We recommend that you approve the striker replacement EO. If you approve, we will prepare the EO for your signature.

Discussion

I. How the Striker Replacement EO Works

A. General Approach: This executive order would require all contracting departments and agencies of the federal government to include provisions in all future contracts (other than collective bargaining agreements) that would (1) prohibit federal contractors and their subcontractors from using permanent replacement workers during a strike; (2) empower the Secretary of Labor to suspend, cancel, or terminate the contracts of any federal contractors who permanently replace strikers during the term of their federal contracts; (3) allow the Secretary of Labor, after a hearing, to debar a federal contractor for violating the EO; and (4) allow the Secretary of Labor, after a hearing, to publish the name of any federal contractor that violates the EO.

B. Coverage Threshold : The reach of the striker replacement EO will be quite limited. Studies indicate that employers resort to permanent replacements in only 14% to 19% of strikes. According to the Bureau of National Affairs, there were 452 reported strikes among all employers that began in 1994. Thus, assuming every employer that experienced a strike was a federal contractor (a very unlikely result), and federal contractors use permanent replacements at approximately the same rate as other employers (roughly 20%), the striker replacement EO would affect only 90 contractors each year in the absence of any dollar threshold.

If you want to further limit the EO's reach, the attached draft could be easily modified to cover only those employers with federal contracts worth in excess of some dollar amount. We estimate that a \$50,000 threshold would exclude better than 80% of all federal

contractors, while a \$1 million threshold would exclude 95%. Using a \$50,000 threshold to exclude 80% of contractors would reduce the number of contractors affected by the EO to 18 per year, while using a \$1 million threshold and excluding 95% of contractors would reduce the number to between 4 and 5 contractors per year. And that is still assuming that every employer that experienced a strike was a federal contractor.

C. Exceptions: The EO empowers the Labor Secretary to exempt (1) a particular contract or subcontract to protect the interests of national security; (2) certain classes of contracts that involve work outside the United States and do not involve American workers; and (3) a contractor, subcontractor, or other vendor upon a showing by the employer of "exceptional circumstances."

D. Enforcing the EO: The EO gives the Secretary of Labor authority to enforce the order and promulgate regulations. The Labor Secretary is required to consult with the contracting agency before taking any action against a contractor. If the head of the contracting agency objects in writing, the Labor Secretary cannot take any further action.

E. Due Process: The EO allows the Secretary of Labor to investigate any contractor, subcontractor, or vendor to determine whether a violation has occurred and to hold any hearings that the Secretary considers advisable. The Secretary must provide a contractor with an opportunity for a hearing before debarring that contractor or publishing its name.

F. Presidential Authority to Issue this EO: The President has the authority to instruct federal departments and agencies with respect to their procurement practices, as long as his instructions are not contrary to law. Opponents will argue that the National Labor Relations Act preempts any action by the President restricting economic activity that should be controlled by the free play of economic forces. The attached legal memorandum (tab 2) gives a fuller discussion of the legal policy questions at issue.

II. Arguments in Support of the EO

A. **Holds unique significance for labor.** The Executive Order will resonate with rank-and-file union activists and leaders better than anything else the Administration can do in the next two years. Labor leaders fought for legislation to bar permanent replacement in the last two Congresses, and many believe the Administration did not work hard enough to break the Republican filibuster last year. As Bridgestone/Firestone continues to hire permanent replacements and the seven-month-old strike there shows no sign of ending, the issue retains great currency. Indeed, striker replacement is a uniquely emotional issue for labor--perhaps comparable to NAFTA--and with this EO you would reconnect your Administration to the time during the 1992 campaign when you walked the line with striking Caterpillar workers. The AFL-CIO and its affiliated unions will certainly support the EO.

B. **Supports cooperative labor-management relations.** The striker replacement EO advances cooperative and stable labor-management relations, a central component of the Administration's workplace agenda. The hiring of permanent replacement workers disrupts the

collective bargaining process--severely undermining labor's negotiating position, extending the length of work stoppages, and sometimes transforming limited disputes into longer and more bitter struggles.

C. Improves overall efficiency of contracts. The EO will enhance the efficient completion of federal government contracts. These contracts require good labor-management relations, and the permanent replacement of strikers precludes such relations. Some empirical evidence supports this conclusion: for example, a 1991 study showed that strikes lasted a mean of 363 days when firms hired permanent replacements, but only 72 days when temporary replacements were hired and 64 days when no replacements at all were used. Since long strikes generally interfere with the efficient execution of contracts, and since permanent replacements lengthen strikes, this EO will further your goal of improving the Federal contracting process. This is the stated premise of the EO.

III. Arguments against the EO

A. Undermines NPR. The EO directly undermines efforts of the National Performance Review (NPR) to streamline procurement systems. NPR has worked to limit paperwork, eliminate unneeded compliance procedures, and in general reduce legal impediments to lowest-bid contracts. In contrast, the EO would require more paperwork and establish additional hurdles for contractors in an already complex process. It would shift emphasis from the outcome--the lowest price for the best goods--to the process, the collective bargaining agreement. (There are particular concerns with regard to Defense contracts. These are often made for specific purposes with specific firms, to which no alternative is available. The EO does allow exemptions "in order to protect the interests of national security," however.)

In addition to these general concerns, the EO is likely to interfere with the progress of NPR's second round of procurement reform. Congressional Republicans will be critical to this round and have indicated significant interest, but they are likely to be repelled by the EO.

B. Slows completion of some contracts. Instances will arise in which the use of permanent replacement workers by a Federal contractor may be the only way to fulfill the contract in a timely manner. While banning striker replacements may be economically sound as a law, this EO could impair the contracting process in individual instances.

C. Appears to be anti-business. The EO may appear to exemplify an "old Democrat" approach, proving to some that the Administration is unsympathetic to business concerns. Many in the business community, especially those who have only tolerated our proposed minimum wage increase, will see the ban on striker replacement as anathema. Their supporters in Congress may press legislation to prohibit funding for the order or otherwise block its enforcement.

D. Faces legal challenge. As noted above, the EO will likely face legal challenges. Some Supreme Court precedents indicate that the EO's action is pre-empted by

the National Labor Relations Act: i.e., activities not explicitly regulated under that Act should be controlled by the free play of economic forces. Congress's rejection of striker replacement legislation in the last two Congresses supports this view, since it reflects a determination not to regulate the area. However, the EO is framed as an exercise of your proprietary (as opposed to policy-making) power, and as such might be safe from court challenge. The outcome would not be certain.

THE WHITE HOUSE

WASHINGTON

FAX COVER SHEET

THE DEPUTY ASSISTANT TO THE PRESIDENT FOR ECONOMIC POLICY
SECOND FLOOR, WEST WING
THE WHITE HOUSE
WASHINGTON, DC 20500
(202) 456-2620
(202) 456-2878 FAX

TO:

Robert Gordon

ORGANIZATION: _____

FROM: GENE B. SPERLING

DATE: _____

NUMBER OF PAGES (including cover sheet): _____

COMMENTS:

see P. 5 & Point II on Page 4.
-PD

The document accompanying this facsimile transmittal sheet is intended only for the use of the individual or entity to whom it is addressed. This message contains information which may be privileged, confidential or exempt from disclosure under applicable law. If the reader of this message is not the intended recipient, or the employee or agent responsible for delivering the message to the intended recipient, you are hereby notified that any disclosure, dissemination, copying or distribution, or the taking of any action in reliance on the contents of this communication is strictly prohibited. If you have received this information in error, please notify us immediately at (202) 456-2620.

THE WHITE HOUSE

WASHINGTON

January 20, 1995

MEMORANDUM TO THE PRESIDENT

THROUGH: Leon Panetta, Robert Rubin

FROM: Gene Sperling

On the minimum wage, there are three decisions that must be made: 1) whether to support a minimum wage increase; 2) if so, how much to increase it; and, 3) when to announce any decision. After several meetings and significant consultation with the Hill, the NEC has come to a single recommendation on the first two issues, while timing still represents a fairly open issue that must be resolved.

I. BRIEF BACKGROUND: The Federal minimum wage is currently \$4.25 an hour. The minimum wage had been frozen at a nominal level of \$3.35 per hour from 1981 to 1990. In 1990, Congress voted to raise the minimum wage by 90 cents -- in two 45 cent stages -- from \$3.35 to \$3.80 in 1990, and from \$3.80 to \$4.25 in 1991. The real value of the minimum wage is now above its value from 1988 to 1990, but is below its value for every other year going back to 1955.

The minimum wage has two important purposes. First, the minimum wage raises the bargaining power for low-wage workers who are not represented by a union and have low skills. The minimum wage may also have a "ripple" effect, whereby wages of workers earning somewhat more than the minimum wage are increased to maintain internal wage standards. As a result, the minimum wage helps many poor and moderate-income families. The second purpose of the minimum wage is that it induces firms to train their workers and take a high-value added/low turnover strategy.

II. EMPLOYMENT AND DISTRIBUTIONAL EFFECTS: The potential effect of a minimum wage increase on employment has been the principal argument raised in opposition to such an increase. While the potential employment effects of a minimum wage increase surely need to be considered, the weight of the empirical evidence suggests that the effect of a moderate raise from its current level is likely to be negligible. Laura Tyson points out that while there is no respectable case for the large job loss figures used by some special interests, there is respectable economic literature that would show a small, marginal job loss. However, Laura and others found most compelling the variety of recent studies examining the effects of raises in the federal minimum wage both across the nation and in particular states, as well as the effects of raising state minimum wages above the federal level.

For example, studies of the federal minimum wage examined the effects of a 90 cent increase in two increments over a two-year period. One of the state studies examined the effects of New Jersey recently raising its state minimum wage by 80 cents, from \$4.25 an hour to \$5.05 an hour; another examined the effects of California increasing its minimum wage 90 cents from \$3.35 an hour in 1987 to \$4.25 an hour in 1988 (which would equal \$5.20 in 1993 dollars). All of these studies found that the minimum wage increases did not reduce employment opportunities. (These studies were conducted by David Card, Alan Krueger, Larry Katz.)

An important point to note about the minimum wage is that while there may be some who are teens or just providing a supplement to a family living comfortably, most are people who are either sole earners for their families or are providing vital support to help maintain a middle income existence. Indeed, 36% of minimum wage workers are the sole earner in their family, while the average minimum wage worker provides nearly 50% of the income in their household.

While increasing the minimum wage does help many people at the bottom of the economic ladder it is also, as mentioned above, important for families where a second income is keeping them barely in the middle class. For example, 43% of minimum wage earners are in the bottom 20% of income, 45% are in the middle 60% -- and only 12% are in the top 20%. Only about one-third of minimum wage earners are teens while two-thirds are adults. Some argue against the minimum wage because it is not as targeted as the EITC toward working poor families. Others find it to be a positive point that an increase in the minimum wage would have such a positive effect on both working poor and middle income households.

III. RECOMMENDATION

NEC Recommendation: The general recommendation from your economic advisors as well as Leon Panetta, George Stephanopoulos and Pat Griffin was to call for a 75 cent increase over two years -- 50 cents the first year and 25 cents the second year -- bringing the minimum wage to a total of \$5.00. The rationale for the two-stage increase to 75 cents is based on both our best estimate of what is sound economically, as well as representing a reasonable political starting point for a minimum wage proposal. From a political perspective, the most important single issue is the degree of support we can gather from Congressional Democrats for our proposal. Several people believe that the best chance for passage is a single 50 cent increase. Pat Griffin believes that we should just go with a single 50 cent increase. Some, such as Gene Sperling, believe that even if we want to end up at a 50 cent increase proposal, we should start with the 75 cent increase so that we have room to bargain and still pass a 50 cent increase. Leon believes a single 50 cent increase has the best chance for passage, but is open to the notion of starting higher to give us bargaining room.

The only other difference is that George Stephanopoulos would prefer to add indexing to the 75 cent increase. Secretary Reich is generally supportive of indexing, but not sure he supports it if it is done from only a 75 cent increase.

a) Economic Rationale: As mentioned above, the economic literature demonstrates that there is good evidence that a minimum wage increase under 90 cents does not have negative employment consequences. While a \$1 increase may still be in the ball park, our feeling is that we would be on stronger footing if our increase was within the levels where the recent economic studies by Katz and Krueger showed no negative employment impact. Furthermore, at \$5.00, the national minimum wage would still be below the highest state minimum wage levels -- New Jersey at \$5.05 and Hawaii at \$5.25.

There was also agreement among most of the economists on the NEC that 75 cents in one year might be too steep and that we were on sounder ground dividing it between 50 cents and 25 cents. Furthermore, a 50 cent increase immediately puts the minimum wage level back up to where it was when the last minimum wage increase passed in 1991. The additional 25 cents increase puts the number up to an even \$5.00. While some may have found a 75 cent minimum wage increase to be small by historical standards, the minimum wage increase you call for must also be considered in the context of the dramatic increase you proposed and signed for the EITC.

b) Political Rationale: As mentioned above, you must consider your recommendation both in terms of the statement it makes and the degree your proposal increases the chance of passage. A higher minimum wage increase is likely to be more satisfactory to those who most support the minimum wage increase -- organized labor and some progressive Democrats. The AFL-CIO calls for a \$1.50 increase -- with three 50 cent increases plus indexing. Sabo and seven Democratic co-sponsors called last year for an increase in the minimum wage to \$6.50, while denying employers a tax deduction for excessive compensation (more than 25 times the lowest compensation paid any other employee). Kennedy also supports a minimum wage increase close to the AFL-CIO recommendation. On the other hand, several Democrats in the Senate have expressed some reservations about proposing a minimum wage increase, and would feel better if we kept the increase to a lower level.

Advocates who argue for a higher number increase state, that since the chance of passage of the minimum wage with the present Congress is considered small by some, the proposal should at least accomplish the political goal of being satisfactory to labor. An argument for going for a lower number -- 50 cents -- is that it would be small enough to lessen intense opposition from some business groups, while responding to the concerns of some Democrats who feel that an increase in the minimum wage goes against the "new Democrat" message. Furthermore, Pat Griffin and others felt that a 50 cent proposal had the best chance of passage.

We felt that a two-stage 75 cent increase without indexing made the most sense from a political perspective as well as an economic perspective. First, while a 75 cent increase would be unlikely to satisfy organized labor and the most ardent supporters of the minimum wage, it would meet your campaign promise of making up the lost value due to inflation since the last minimum wage increase while adding 25 cents to spare, and it seems to be a level that could hold most Democrats in Congress together. Finally, to the degree that a one-time 50 cent increase represents the proposal with the best chance of passage, a 75 cent proposal gives us some negotiating room.

IV. INDEXING: The proposal that was considered for indexing would tie the minimum wage to the wages of the median worker or the 25th percentile worker. These standards are preferable to indexing to the CPI because they would avoid contributing to an inflationary cycle that could result if the CPI was used. The arguments for indexing are that it would protect the value of the minimum wage without making Congress continually have to seek new legislation. Politically, Republicans who oppose indexing would be put in the position of having to support indexing the capital gains tax cut for well-off Americans while opposing indexing for wages for workers at the lowest wage levels.

Nonetheless, the NEC and White House staff felt that a 75 cent increase was adequate without indexing. The arguments against it were the low chance of passage, the risk that it would be perceived as inflationary (even with our attempts to index to a measure other than the CPI), and the concern that the perceived benefit to workers would not be large enough to overcome the political downsides. Furthermore, even strong advocates of a stronger minimum wage increase might not support an indexing proposal because they would fear that indexing after only a 50 cent or 75 cent increase would lock them into too low of a level for the future. Bob Rubin also stressed that while business groups would oppose us on a minimum wage increase, if indexing were added it would add significant intensity to that opposition that would work against us on this as well as other business-related matters.

V. SUB-MINIMUM WAGE:

The NEC also discussed the issue of adding a sub-minimum wage for teenagers. There was a three-year trial subminimum wage in the 1989 minimum wage increase, (15% less for teens for up to 6 months), but the results were that it was hardly used for several reasons -- including recordkeeping requirements. Because the impact was so minimal, some might claim that we should go ahead and do this. Yet, the decision of the NEC was that in light of that de minimis impact, there was no economic rationale to justify the problems a subminimum wage proposal would create with those likely to support passage of a minimum wage increase.

VI. ARGUMENTS AGAINST NEC RECOMMENDATION: Despite the fact that the NEC was virtually unanimous in its recommendation, we wanted to give you "cons" -- the opposing arguments you are likely to hear for either not increasing the minimum wage or, on the other hand, calling for a larger increase.

- **Hurts New Democrat Message:** Some Congressional Democrats believe that this works against the "new Democrat" message -- as an increase in the minimum wage is perceived as a traditional Democratic/labor agenda item and is likely to be vigorously opposed by small business. Arguing against this concern is the fact that while there will be intense small business opposition, polls consistently show that 70% of Americans support an increase in minimum wage. Other Democrats concerned about the minimum wage have argued that if we do propose a minimum wage that we package it together with other policies designed to increase wages for working Americans.

- **Will Create Opposition without Creating Strong Support:** A 75 cent increase is likely to run the risk of stirring strong small business opposition without generating strong support from organized labor which is likely to feel it is far too low. Arguing against this is the degree that we can work with Democrats to work together to draw a line on the side of working Americans, against Congressman Armey and others who strongly oppose this popular issue.

- **Unfunded Mandates:** An increase in the minimum wage does affect some state and local governments who do pay the minimum wage for some jobs and therefore could claim that this is an unfunded mandate.

VII: TIMING: The main timing question is whether or not to announce your minimum wage decision in the State of the Union.

Pro:

- The State of the Union allows you to directly make your case over the heads of the special interests to the general public on an issue where the general public is with us.
- The State of the Union allows you to blend the minimum wage in with an overall strategy to raise incomes for working people.
- There has been considerable speculation about how we are going to decide this issue -- waiting past the State of the Union continues that process -- going earlier may distract from the build up to the State of the Union.

Con:

- A minimum wage increase in the State of the Union might be treated as a major news item that could distract from the basic messages in the State of the Union.
- There is still time to announce it prior to the State of the Union (though it would have to be almost immediately) or after it as a way of keeping our economic story going or building up to rewarding work for the welfare working session.
- There is some evidence of increasing anxiety about doing this among Congressional Democrats.
- There was general agreement in the last NEC meeting that this announcement should be in the State of the Union -- though there exists today significant disagreement on this issue within the White House.

Sperling.

THE WHITE HOUSE

WASHINGTON
August 30, 1995

MEMORANDUM TO THE PRESIDENT

FROM: LAURA TYSON
BO CUTTER

SUBJECT: PROPOSED EXECUTIVE ORDER REGARDING MINIMUM
WAGE

We oppose an Executive Order requiring federal contractors to pay a minimum wage higher than the statutory minimum wage. (Gene Sperling is out of the country, but we believe he would agree.)

- . As a matter of process, we should not make as complex a decision as this one with as little analysis as has been carried out to date.
- . The proposed Executive Order would further complicate federal procurement, raising an additional barrier to working with the Federal Government, and would be inconsistent with the overall direction of federal procurement policy. We have not analyzed the long-run costs the Government would experience as firms shift away from federal work.
- . The proposed Executive Order would raise federal procurement costs, and, therefore, because budgets will not expand, may well result in lower employment derived from federal procurement.
- . The proposed Executive Order raises a number of other detailed issues we have not been able to analyze in this short a time period: How would the international operations of affected firms be treated? Would firms cut back on benefits? Are we legally able to terminate contracts?
- . Finally, the basic justification for such an Executive Order -- that it would increase overall economic efficiency -- is not supportable for a measure applying only to part of the economy. Larry Katz, who is, as you know, a leading proponent of this argument when applied to the whole economy, would probably publicly criticize it in this case.
- . We think our current minimum wage position is right and a political winner. We do not need to jeopardize our position with one action we have not thought through. If you wish, we can initiate a process immediately to develop a more thorough analysis and provide you with a better basis for a decision.

not changed
since 2/20

DECISION MEMORANDUM FOR THE PRESIDENT

From:

Subject: Future Direction of Your G.I. Bill for America's Workers

This memorandum presents options for a decision on the content and structure of the second-term G.I. Bill initiative.

BACKGROUND. In December 1994, you proposed a Middle Class Bill of Rights to empower working Americans to pursue a lifetime of learning through education and training tax deductions, tax credits for families with children, and expanded IRAs. The fourth point of your Middle Class Bill of Rights was the G.I. Bill for America's Workers. In your 1995 State of the Union message, you articulated the vision as follows:

"The New Covenant approach to governing is as different from the old bureaucratic way as the computer is from the manual typewriter... The old way dispensed services through large, topdown, inflexible bureaucracies. The New Covenant way should shift these resources and decision-making from bureaucrats to citizens, injecting choice and competition and individual responsibility into national policy... We should pass a G.I. for America's workers. We propose to collapse nearly 70 federal programs, and not give the money to the States, but give the money directly to the American people; offer vouchers to them so that they can get a voucher worth \$2,600 a year for up to two years to go to their local community college or wherever else they want to get the skills they need to improve their lives. Let's empower people in this way. Move it from government directly to the workers of America."

The actual proposal was far more complex. As detailed in your FY 1996 Budget, it increased funding for these activities by X% and combined 70 employment and training programs into one workforce development system - - not one program - - with five discrete component parts (see consolidation schematic at Tab A):

- (1) **Individual Skill grants.** Financed at \$3.6 billion in the Labor Department, vouchers of up to \$2,620 would support "technical education" for dislocated workers and low-income persons. (\$2.1 billion of the amount was derived by transfer from Pell grant funds)

used then (and now) for these purposes. *Didn't this represent percent for some contribution*

(2) **Individual Pell grants.** Financed at \$4.5 billion in the Education Department, grants of up to \$2,620 would provide student financial aid to defray the costs of associate's and bachelor's degree courses. Pell would no longer be used for non-degree training.

(3) **A grant to States for adult services other than training.** Financed at \$2.7 billion in the Department of Labor, this grant would support a State and local system of job placement and training-related services provided through one-stop career centers, with a limited national reserve for activities such as grants for multi-State mass layoffs, and research. This was the major consolidation of the Labor Department's Job Training Partnership Act (JTPA) and the Employment Service. *How many*

how many
(4) **Two State grants for youth.** Financed at \$2.9 billion, one grant would support vocational education for in-school youth through the Education Department; a second grant for at-risk and out-of-school youth would offer second chance training and work experience through the Labor Department. All activities were to be structured within the School-to-Work framework jointly administered by the Education and Labor Departments.

(5) **A State grant for adult and family literacy.** Financed at \$490 million in the Education Department, this grant would provide GED, ESL, and basic skills instruction, as determined by the States.

Only the law were
The FY 1996 Budget proposed \$14.2 billion for the G.I. Bill for America's Workers, an increase in overall funding of \$1 billion above 1995 (see resource table at Tab B). We estimated that the Skill grant part of this approach (\$3.6 billion) would serve all dislocated workers who wanted training, but only serve some of the economically disadvantaged adults who needed and wanted training. As a result, State and local grantees would be required to ration Skill grant resources. (It was (and remains) impossible to distinguish clearly between Skill grant and Pell grant eligibility on the basis of individual characteristics, so these take-up rates are very rough estimates.) Both degree and non-degree training and education would have remained financible through student loans and income-contingent repayment, but we did not factor these resources into the discussion.

LEGISLATIVE HISTORY. The Administration did not transmit legislation to authorize the G.I. Bill reforms, except for a separate bill in May 1995 to reauthorize the vocational and adult education programs. We chose instead to work informally with the 104th Congress on bills Republicans were moving through both chambers. Our judgment was that specific Administration bill language would raise issues our supporters could not accept and would draw fire from Republicans unnecessarily. Senator Kennedy supported this approach.

The proposal to move Pell resources to the Labor Department was abandoned almost

immediately because it was opposed vigorously by the higher education community and many in Congress on both sides of the aisle.

In the Fall of 1995, training reform bills -- known as "CAREERS" (Goodling) and the "Workforce Development Act" (Kassebaum) passed both Houses of Congress with overwhelming bipartisan support (345-79; 95-2). The Administration expressed conditional support for both bills and organized Democratic and interest group support despite concerns with each. We wanted to keep the issue alive in Congress and looked to conferees to address concerns. This also helped us in the appropriations fight, where we could argue that it made no sense to cut funding deeply with a major reform on the horizon. Of the two bills, Rep. Goodling's CAREERS was closer to fulfilling your G.I. Bill principles.

CAREERS required, with an exception for training run by community-based organizations, vouchers for adult training, "report cards" and performance standards for training programs, one-stop and school-to-work frameworks for adult and youth programs (although it would have repealed the School-to-Work Act), and private sector involvement in workforce development programs. By contrast, the Kassebaum bill would make vouchers available at State option; authorize a single State grant with a 25% "flex pot" for State-determined workforce development activities, which could include supporting company training of the employed; weaken accountability by permitting States to define success in their own terms; and greatly diminish the role of local communities in determining training needs.

As the two bills went to conference, the fierce FY 1996 and 1997 appropriation struggles were underway. The ~~appropriation negotiations~~ led the Administration to advocate financing for dislocated workers of at least \$1.3 billion, and to fight to preserve funding for existing categorical programs for summer jobs and vocational education, which had been cut severely by both chambers. With the help of constituent groups -- including organized labor's support for dislocated worker funding -- the Administration won the appropriations battles. However, in the process, resulting of necessity, the G.I. Bill reform agenda became less specific on both consolidation and the form of Skill grants.

In a May 1996 letter to the conference leadership (attached at Tab C), you urged the conferees to craft a bipartisan bill that incorporated your G.I. Bill principles. You ^{also} advocated earmarked funding for dislocated workers and "properly targeted" resources for a summer jobs program, adult education and training, in-school youth, at-risk youth, and the labor exchange. Your original G.I. Bill principles never explicitly stipulated these elements as essential components.

Pressured by conservative "family groups" to resist compromise, and for other reasons, Republican conferees excluded the Administration and the minority from the negotiations. Some of the majority conferees believed the Administration was negotiating in bad faith, or defending the status quo. The partisan conference produced a bill that resembled Kassebaum's flawed block grant approach. In part, the conference bill was unacceptable because it required only a 50-State

training voucher "pilot," failed to ensure that adequate resources would be available for adult training, and included weak accountability provisions. Former Chief of Staff Panetta made an effort to re-open negotiations. The last effort, a June 17th offer from the Administration representing our "bottom line issues," (attached at Tab D), received no response from the conferees. Emerging in July 1996, the conference bill failed to gain the Administration's support or the vote of any minority conferee. The bill never reached a floor vote.

ADMINISTRATIVE REFORMS. As we consider strategy for a new effort, it is important to recall that we already have made some progress toward achieving your G.I. Bill objectives. To prepare for the comprehensive legislative reforms, the Labor and Education Departments have aggressively pursued training and employment reforms through administrative changes and other statutory authorities. Initiatives include:

- **One-stop career centers.** Begun in 1994, this DOL initiative consolidates multiple training and employment programs at the "street level" through competitively awarded State implementation grants. The number of States implementing one-stop systems will grow from 16 currently to 43 in by the end of 1997. In 1998, all States will be implementing one-stop systems. *Should this be made a multi-Statewide?*
- **America's Job Bank and America's Talent Bank.** These two rapidly expanding DOL Internet websites now provide access to 600,000 job openings and resumes of 2 million job seekers, respectively. The extremely popular America's Job Bank has grown from 250,000 "hits" in 1994 to 8.5 million in 1996. We do not know the extent to which actual hires result from a hit, but the growing volume of usage suggests workers are using it to their benefit. *more accurate* *45 or 6*
- **School-to-Work opportunities.** Since enactment in May 1994, the School-to-Work Act has provided the "seed capital" to spur State school-to-work systems that connect secondary education to work-based learning, postsecondary training, and career opportunities. Currently 37 States are receiving implementation grants; in 1998, all States are expected to be implementing their School-to-Work systems.
- **Waivers and funding transfers.** With the Administration's support, the FY 1997 appropriation act provided unprecedented flexibility for State and local employment and training programs, as a first step toward enactment of comprehensive reform legislation. (You had already obtained significant new waiver authority for Education Department programs in 1994.) The Budget continues this flexibility in FY 1998, which includes:
 - **Waiver authority** to permit the Labor Secretary to waive a wide range of JTPA and Wagner-Peyser Act (i.e. Employment Service) statutory and regulatory provisions pursuant to a request submitted by a State, in return for improved performance.

- **“Work-Flex” partnership demonstration** (modeled on the 1994 “Ed-Flex”), in which up to six States are authorized by the Labor Secretary to waive JTPA and Wagner-Peyser provisions, pursuant to a plan describing the local waiver process, outcomes to be achieved, and assurances of fiscal accountability.
- **Funding transfer authority** to permit Governors to approve requests by local programs to transfer up to 20% of funds for the dislocated worker and low-income adults between the two JTPA programs. Since FY 1996, unlimited funding transfers have been permitted between the JTPA Summer Jobs and year-round youth training programs.

RELATED 1998 BUDGET PROGRAMS. The context is also shaped by several of your new proposals. The FY 1998 Budget contains several new sources of funds targeted at the same population as the G.I. Bill.

- **Pell expansion and new coverage.** More than one-third of all Pell grant resources finance technical training, such as Skill grants were to do. The FY 1998 Budget proposes to raise the maximum Pell Grant award by \$300, to \$3,000, marking the largest increase in two decades, and to expand eligibility of students generally aged 24 or older. These proposed changes would bring in about 348,000 more students into the program, reaching a total of over four million low- and middle-income students. Many of the new Pell recipients are the older unemployed seeking training, for whom Skill grants were proposed.
- **HOPE scholarships.** These proposed tax credits are available for degree or certificate programs, allowing them to finance many of the job training programs offered by community colleges. They would provide families up to a \$1,500 per-student tuition tax credit each year for two years of postsecondary education and training.
- **Tuition tax deduction.** This deduction is even broader than your proposed tax credit, allowing deduction of tuition for any education for improving or acquiring job skills. The FY 1998 Budget proposes to give families a tax deduction worth \$5,000 a year in FY 1997 and FY 1998, and \$10,000 a year in FY 1999 and thereafter for postsecondary education and training costs to promote lifelong learning.

G.I. BILL IN THE FY 1998 BUDGET AND 105TH CONGRESS. The FY 1998 Budget reiterates support for the G.I. Bill principles, characterizes training reform as “essential,” and anticipates working with the 105th Congress to produce a bill. For comparative purposes, using a program mix matching the original G.I. Bill in the FY 1996 budget, the FY 1998 Budget request for G.I. Bill programs is \$14.3 billion (\$4.9 billion in Labor, \$9.4 billion in Education),

\$109 million above the FY 1996 Budget request. The non-degree postsecondary education supported by the Education Department's Pell grants (which totaled \$2.1 billion in FY 1996 and was proposed to be transferred to Labor) continues as a major contributor to technical education and training. It no longer is considered part of the G.I. Bill/Skill grant mix.

The FY 1998 Budget makes no specific statement about the number of programs to be consolidated. The original G.I. Bill consolidated 70 training and employment programs for (1) in-school youth; (2) out-of-school youth; and (3) adult education and literacy; and (4) adults. Since 1996, 33 of the original 70 programs have been collapsed through administrative reforms, appropriations actions, and other means. Soon to be transmitted to the 105th Congress, the Education Department's legislation to reauthorize Vocational Education for in-school youth and the Adult Education Act would continue this streamlining. [Optional detail follows on the components of the "4 to 1" schematic.

- **In-school youth** program consolidation will occur in the Education Department's bill to reauthorize the Perkins Vocational Education Act, soon to be transmitted to the 105th Congress. This bill will eliminate categorical program authorizations and include strong coordination requirements with out-of-school youth programs and the School-to-Work initiative.
- **At-risk youth** programs in the Labor Department will not be consolidated at the Federal level. At the State level, coordination will occur through the use of waivers, funding flexibility, and implementation of School-to-Work systems.
- **Adult Education** program consolidation will occur in the Education Department's pending reauthorization bill, which would streamline the 12 existing program authorizations into a single State grant and a national authority.
- **Adult program** consolidation will hinge on the direction of Skill grants in your second term G.I. Bill.]

Training reform legislation is a priority for the 105th Congress. In the Senate, a Daschle bill to consolidate adult training programs (S. 17) was introduced on January 21st. This bill establishes a State training voucher system. In the House, hearings on training reform began on February 11th; Labor may be asked to testify on March 4th.

POLICY OPTIONS. Policy options are presented below on the nature of the voucher to pursue in a second-term G.I. Bill. Each option would require new legislation; each also assumes strengthened "gatekeeping" (efforts to ensure high quality training) and consumer reporting of training program performance to ensure accountability for results.

You consistently have advocated a voucher to empower adults served by JTPA -- dislocated workers and low-income individuals with little work experience -- with the resources

and information to choose their own training. Vouchers have been one of the most prominent of the five component parts of the G.I. Bill proposal.

Current programs pay for much more than training. In fact, funds used exclusively for training (a proxy for what would be converted to Skill grants) comprise less than half of the original G.I. Bill programs funds in the DOL JTPA programs. The remaining non-training dollars would finance State grants for a workforce development infrastructure of one-stop career center systems and the labor exchange, local workforce boards, gatekeeping and consumer reporting activities, training support services (such as job counseling), and non-vouchered on-the-job training. These remain key features of the G.I. Bill concept.

The Issue: Nature of your Skill grant proposal.

Exclusive of Pell grants and Hope, your FY 1998 Budget includes \$2.4 billion for adult JTPA programs, of which \$1.3 billion is for dislocated workers and \$1.1 billion is for low-income adults, as follows:

- **Dislocated worker assistance** of \$1.35 billion would serve about 605,000. The cost per participant is about \$2,150. Only about half of participants receive -- and resources finance -- training (\$675 million). The remaining \$675 million finances job search assistance, other training-related and support services, and administration.
- **Low-income adult** resources include \$1.1 billion to serve about 350,000. The cost per participant is about \$3,000. Only about \$600 million of the \$1.1 billion would finance training; the remaining \$500 million provides counseling, support services, and related services.

The eligible population -- 29 million low-income adults and 3 million dislocated workers far outstrips available resources. The full 29 million was never the focus of your G.I. Bill. If all eligibles received a Skill grant, expenditures would total \$x.x billion, compared with just \$1.2 billion proposed for training in your FY 1998 Budget. Currently, discretionary appropriations limit JTPA training expenditures; access to these resources are rationed through statutory eligibility rules and other discrete State and local decisions about who will receive services. (Pell grants also are rationed by multiple eligibility screens and award limits, but with much less local agency -- ie: school -- discretion.) Both of the Skill grant options described below would require rationing of resources in one form or another.

Option A. Federal Skill grant. Your original Skill grant proposal did not eliminate substantial resources for nontraining services for adults, such as work preparation, counseling, and support services. While it is true that some people receiving only support services and counseling in JTPA might be as successful solely with a training grant as many are in Pell, your proposal presumed that disadvantaged adults and many dislocated workers in fact would continue to need more than training. The option below maintains this approach.

This option would create a national Skill grant of up to \$3,000, similar to the Pell grant program. In effect, it would take up where Pell grants leave off: Funding would be made available for short-term, non-degree training (currently available in JTPA, but not in Pell) and for skill training for dislocated workers through a "prospective income" calculation that disregards their pre-layoff earnings. These Skill grants would be available to individuals at one-stop career centers, JTPA's current community-based system of training providers, and wherever Pell grants currently are accessible (virtually every accredited school). It could be administered (i.e., vouchers cashed) either by the Labor or Education Department, but divorcing the funds from the other adult counseling and related services would add a major complexity.

Rationing would have to occur to stay within the Budget. Substantial demographic and work test processes would, as was presumed in FY 1996, narrow eligibility. For example, in FY 1996 we assumed all dislocated workers would receive job search assistance prior to qualifying for a Skill grant; this had the effect of limiting the number of Skill grant recipients to less than 300 thousand of the 2 million eligibles. For disadvantaged adults even tighter eligibility screens would have to be established (MORE WORK NEEDED HERE). Fund rationing options could include:

(1) imposing eligibility screens sufficient to reach a population estimated to expend the funds available but, as in Pell, honor all vouchers claimed (i.e., the appropriation would estimate, but not control, outlays).

(2) if tighter eligibility screens are considered unacceptable, then honoring claims for vouchers from eligible individuals at eligible schools on a first come, first served basis;

Pros:

- Most consistent with eliminating the role of State and local bureaucracies, and most like Pell grants.
- A bold, sweeping reform proposal that would be seen as more dramatic than the Republicans' more modest reform via State block grants with optional training vouchers.
- If Skill grants are limited to tuition costs, they would leverage Federal dollars with State, local, and private resources. JTPA contracts are not limited to tuition costs alone.

Cons:

- New eligibility screens would necessitate a significant reduction in current JTPA eligibility rules for training.
- Strongly opposed by Governors. They want a no-strings workforce development block grant. And to date, they only support optional, not mandatory training vouchers. They may also want to use these funds to support welfare reform.

- Strongly opposed by mayors, county commissioners, community-based organizations, public employee unions, and all stakeholders in the current training system.
- Congress is proceeding on a "consensus" bill, more like CAREERS. A radical new national skill grant proposal could jeopardize our role as partner in these negotiations and shift influence to those who advocate a block grant with no mandatory vouchers.
- Could reduce the possibility of achieving a consensus bill with the 105th Congress that includes more modest, yet meaningful reforms.

Option B. State/local Skill grant. This option continues the approach we advocated in our negotiations with the 104th Congress. An adult grant to the States would include an earmark of \$1.1 billion for dislocated worker assistance and finance training and training-related services for low-income adults. A separate State grant would finance the Wagner-Peyser labor exchange, which would operate through the one-stop centers. All training would be financed through skill grants, which would be available only at one-stop career centers at the discretion of local program operators. Within broad federal parameters, States and local boards would ration as they do now - - by allocating training (now in the form of vouchers) to only a small share of potentially eligible dislocated workers and low-income adults.

Pros:

- Builds on the administrative reforms already underway, described above.
- Supports important constituencies who stood with us through the budget battles last year, and who would be deeply offended by a change in policy.
- Is the option most acceptable to key Democrats.
- Advances the position we argued with training reform conferees in the 104th Congress; could enhance the prospects for enactment in this Congress.
- Ensures individuals get labor market and training provider performance information at one-stop centers to help them make wise training choices with their vouchers, and any necessary support services and follow-up services to promote training success.

Cons:

- Is one step removed from full empowerment of eligible individuals, by requiring them to seek vouchers through local program operators.
- Empowers State and local bureaucracies, not individuals, to decide who gets a Skill grant.

Recommendations:

[not yet written]



November 12, 1996

MEMORANDUM FOR LAURA TYSON
 GENE SPERLING

FROM: PAUL DIMOND *AD*

SUBJECT: SEPARATING G.I. BILL PROVISIONS?

CC: BRUCE REED

If you do not think it is possible to achieve a single, integrated education and training account to achieve the President's goal of putting good information and increased purchasing power in the hands of individuals and families, Part I elaborates an alternative approach that retains the several funding streams but coordinates their implementation. The major issues are: (a) the amount of budget resources you want to place in each stream, the total education and training budget and the extent to which you want to place these funding streams on the mandatory side of the budget, including as refundable tax credits; (b) the extent of the coordination between funding streams, both in terms of the users and the administration and gatekeeping; and (c) whether you wish to add non-degree programs as permissible uses of these funding streams. The purpose of this analysis is to raise key issues so that the President is not blind-sided by the current budget proposals of DoED and DoL that fail to implement the key principles of individual empowerment, market accountability, and rewards for performance.

Part II proposes a workable alternative to bring the youth programs in line with the President's basic principles.

The premise underlying both parts is that we cannot and should not again propose a single G.I. Bill for America's Workers authorizing legislation that seeks to tie all DoEd and DoL youth and adult education training and job search programs together. That approach did not work in the last Congress and will not work in this Congress: it will only invite unnecessary battles with the Republican Right Wing about School-to-Work and Republican centrists about devolving all education and training to the states.

I. Adults

Hope scholarship -- refundable tax credit for education and training, degree and 1-year certificate programs. \$1500 for two years, including 1-year certificate. [Issues: raise to \$2500 per year? Include non-degree programs? Information include percentage and time for students to achieve degree or certificate (and, if include non-degree programs, job and income results for students in non-degree programs)? Gatekeeping? Administer through DoEd student financial assistance, with advance payment of refundable portion credit? How coordinate with IRS?]

Education tax deduction -- for education and training, degree and 1-year certificate \$10,000. [Issues: include non-degree?]

Dislocated Worker Skill Hope Credits -- after 12 weeks of job search, refundable tax credit. Total of \$2500 [including \$1500 Hope Scholarship]. [Issues: how relate to portable health care? Raise amount to \$3000? DoEd student financial assistance administer, with UI/ES confirming 12 weeks of job search? Include non-degree?]

Pell Grant for degree and 1-year certificate, [Issues: mandatory or discretionary? increase to \$3000 or \$3500, perhaps in exchange for limiting to first two years? Add non-degree? gate-keeping and information?]

Student loans, with Pay-As-You Earn and 25-year sliding scale repayment plans [Issues: include non-degree? how set bar and conditions of GSL and Direct Lending to make loans more affordable and convenient to students, with better information, gate-keeping, and collection?]

[Issue=\$250 refundable credit for job-search? or rely on interactive job banks and counseling/placement from the search firms that represent employers?]

[Workforce Development Act -- if omit non-degree from Hope Scholarship, Pell Grants and Student Loans, then go with principle of devolving DoL programs to states, with states having flexibility to design individual grants for job search and training, with sign-off by local labor market workforce boards made-up of majority of private employers and by county-city executives; approval by Secretary of DoL in consultation with Secretary of Education]

[Welfare-to-Work Jobs Challenge based on principle of state-local design to connect welfare-to-work participants to real jobs in expanding local labor markets]

2. Youth Education and Training

DoL: performance incentive awards to states and localities that put per pupil K-12 resources behind students 17-24 without high school diplomas to learn to earn high school diploma, workplace skill and (a) job or (b) access to post-secondary education. E.g., \$1000 per student with \$500 to state-locality for each student they get back into learning program that meets conditions and another \$500 for each such student earning a high school diploma, workplace skill certified by local workforce board and (a) job with 1500 hours work per year or (b) access to post-secondary education. [Issue: need authorization? if so, don't tie in any way to School-to-Work so that R's don't have to face issue of right-wing attack on STW. Also: assume that keep summer jobs, Job Corps; small fund for experiments, demos?]

Vocational Education/ACE Graduation Challenge: incentive awards for retaining more students in "school" until earn high school diploma that means something to employers and colleges. Use bully pulpit to encourage range of choices, apprenticeships, experienced base learning, charter schools, etc.

continue to fund and implement STW, but use bully pulpit to coordinate with new DoL incentive awards and DoEd graduation challenge.

E X E C U T I V E O F F I C E O F T H E P R E S I D E N T

12-Dec-1996 10:22am

TO: Gene B. Sperling

FROM: Paul R. Dimond
 National Economic Council

CC: Kenneth S. Apfel
CC: Barry White

SUBJECT: "Incumbent Worker" Training Proposal

Gene,

However styled -- a categorical program or a maximum setaside in a block grant to the governors -- this is a bad idea. It appeared out of nowhere in the Senate version of the Workforce Development Bill -- permission to Governors to tap up to 50% of the "Flex" portion of the block grant for incumbent worker training. [The House Careers Bill had no such provision.] Kassebaum thought Senator Kennedy was the source of this, and Kennedy thought the governors had demanded that Kassebaum include this. After inquiry, it appears that this provision came from some very old DoL ideas from a bygone era, when some thought it made sense to invest in incumbent worker training as a way to make "failing firms" competitive -- which, of course, is a lose-lose proposition.

Following the inquiry, Senator Kennedy said the provision was no idea of his (and he thought it was subject to great abuse and should be eliminated entirely). Kassebaum agreed with this position. Governor Voinovich personally told me it was a terrible idea because all it did was put pressure on governors to put scarce funds into "worker training" in "failing firms" that wanted a "bailout political favor" from the governors. And DoL fought like crazy to get the provision out of the senate version entirely. It was eliminated entirely.

This is an uneconomic, bad idea all around: stick to the real incentives for incumbent working training -- firm self-interest, complete deductibility of all training expenses (although some public firms wish these expenses were instead given less favorable tax treatment and capitalized rather than expensed so that their annual profits look bigger), and expand Section 127 expensing. You know the drill on this: don't let DoL reopen a can of worms (that I suspect they tried last year behind the scenes and then pulled back from when they realized what a bad idea it was). Join Ken in Killing this bad, old idea immediately in the budget process before DoL shoots itself (or our leader) in the foot again.

Last spring, I did propose considering an alternative for firm-training: permitting the flexible state-designed training voucher to be cashed in by "growing firms" who hire dislocated or otherwise unemployed workers

(including welfare mothers), subject to the same gatekeeping requirements as qualifying non-degree training programs at education and training providers i.e., an earnings test from U.I. records for the year following the training whether at the hiring firm or the training provider. Please note, however, that even this proposal merely builds on what you always knew was and is the fundamentally conflict in any of the congressional bills with the President's basic vision for the G.I. Bill -- this proposal is merely another aspect of a vague and variable state-designed voucher approach (with lots of exceptions to permit state-contracted training) AND the likelihood that Congress would limit even this very watered down version to only dislocated workers. The G.I. Bill in congressional authorizing committees was last year and will again this year be so ground down that the President's commitment to clear, federally defined, and assured vouchers for post-secondary education and training won't be implemented.

So do whatever you can on the mandatory side: that's where the Presidential legacy -- and the real dollars and on-going federal commitment are -- for federal vouchers for post-secondary education and training for all Americans (including "unemployed and underemployed" and "dislocated and disadvantaged workers") is going to have to be won.

Paul

7 pages - b7d

September 14, 1995

MEMORANDUM FOR GENE SPERLING
TOM O'DONNELL

FROM: Ellen Seidman

SUBJECT: Archer Pension Raid Proposal

Section 13607 of Chairman Archer's bill (page 127), described in item 9 of the summary (page 15), would allow employers to take money out of marginally over-funded pension plans "for any purpose." This is a blatant raid on workers' pension money, and goes entirely contrary to what Congress achieved in the Retirement Protection Act, passed as part of GATT last December, which was meant to ensure that employers would fund their pension plans and keep their promises to their employees.

IT IS CRITICAL THAT WHATEVER STATEMENT THE PRESIDENT MAKES BLASTING THE ARCHER PACKAGE INCLUDES A CLEAR AND UNAMBIGUOUS REJECTION OF THIS PROPOSAL.

In the 1980s, over \$20 billion was taken out of pension plans through "reversions." When the economy and corporate fortune turned at the end of the decade, many of those plans were left underfunded, which led Congress to stop the raid. This proposal would start it all over again.

It is not only lousy retirement policy, it is lousy tax policy (it enables rich employers to use their pension plans as a tax shelter).

Archer will justify the proposal on the grounds that the plans would still be overfunded. However, the assumptions used in calculating whether they would be have been shown by the PBGC to significantly understate what would be needed to pay workers if the plan terminated. And the GAO found that even the PBGC calculation underestimates what happens in the real world when a company gets into financial trouble and has to terminate its pension plan.

The AFL-CIO was lobbying heavily against an earlier rumored version of this proposal, which would have limited the use of the pension money to health care. They are presumably going ballistic now. Mr. Gibbons blasted the proposal on the floor this evening. Alice Rivlin also sent up a letter on the earlier version.

Attached are:

- o Archer's description of the provision
- o Alice's letter
- o A short rhetorical diatribe on the provision that could be used by the President, Gephardt or someone else

Description of Proposal

The proposal would provide that where the taxpayer satisfies the replacement property requirement of section 1033 by acquiring stock in a corporation, the corporation generally would reduce its adjusted bases in its assets by the amount by which the taxpayer reduces its basis in the stock. The corporation's adjusted bases in its assets would not be reduced, in the aggregate, below the taxpayer's basis in its stock (determined after the appropriate basis adjustment for the stock). In addition, the basis of any individual asset would not be reduced below zero. The basis reduction first would be applied to (1) property that is similar or related in service or use to the converted property, then (2) to other depreciable property, then (3) to other property.

The application of these rules can be demonstrated by the following examples:

Example 1.—Assume that a taxpayer owned a commercial building with an adjusted basis of \$100,000 that was involuntarily converted, causing the taxpayer to receive \$1 million in insurance proceeds. Further assume that the taxpayer acquires all of the stock of a corporation, the sole asset of the corporation is a building with a value and an adjusted basis of \$1 million, and the stock acquisition qualifies as the acquisition of replacement property. Under the proposal, for section 1033 to apply, the taxpayer would reduce its basis in the stock to \$100,000 (as under present law) and the corporation would reduce its adjusted basis in the building to \$100,000.

Example 2.—Assume the same facts as in Example 1, except that on the date of acquisition, the corporation has an adjusted basis of \$100,000 (rather than \$1 million) in the building. Under the proposal, the taxpayer would reduce its basis in the stock to \$100,000 (as under present law) and the corporation would not be required to reduce its adjusted basis in the building.

Effective Date

The proposal would apply to involuntary conversions occurring after September 13, 1995.

9. Corporate pension reversions

Present Law

Under present law, defined benefit pension plan assets generally may not revert to an employer prior to the termination of the plan and the satisfaction of all plan liabilities. Any assets that revert to the employer upon such termination are includible in the gross income of the employer and subject to an excise tax (sec. 4980). The rate of the excise tax generally is 20 percent, and is increased to 50 percent unless the employer maintains a replacement plan or makes certain benefit increases in connection with the plan termination.

08/14/88 THU 18:55 FAX 202 328 4018

PBCC/OED

004

transfer of excess assets from a defined benefit pension plan (other than a multiemployer plan) to the employer. Amounts transferred could be used by the employer for any purpose. Amounts transferred would be includible in the gross income of the employer and generally would be subject to a 6.5-percent excise tax. No excise tax would apply in the case of transfers occurring before July 1, 1996.

A transfer would not affect the plan's qualified status and would not be considered a prohibited transaction. There would be no limit on the number of such transfers that could be made during any taxable year.

In order for the transfer to be qualified, the accrued retirement benefits of participants (including participants who separated from service during the 1-year period ending on the date of the transfer) under the pension plan must be nonforfeitable as if the plan terminated immediately before the transfer. The other requirements under present law for qualified transfers to pay qualified current retiree health liabilities (e.g., the maintenance of effort requirement) generally would not apply.

Excess assets would be defined as under present law, and would be determined as of January 1, 1995, or, if January 1, 1995, is not a plan valuation date, as of the last plan valuation date preceding January 1, 1995.

The proposal would not apply to transfers in taxable years beginning after December 31, 2000.

Effective Date

The proposal would be effective January 1, 1995.

10. Modify tax benefits for ethanol and methanol from renewable sources

Present Law

Present law provides several tax benefits for ethanol and methanol produced from renewable sources (e.g., biomass) that is used as a motor fuel or that is blended with other fuels (e.g., gasoline) for such a use. These benefits are--

(1) A 54-cents-per-gallon (60 cents per gallon for methanol) blender income tax credit;

(2) A 5.4-cents-per-gallon (6 cents per gallon for methanol) excise tax exemption from the motor fuels' excise taxes; and

(3) In the case of ethanol, a separate 10-cents-per-gallon credit for small producers, defined generally as persons whose production does not exceed 15 million gallons per year

Upon plan termination, the accrued benefits of all plan participants are required to be 100-percent vested.

Under present law, a pension plan may provide medical benefits to retirees through a section 401(h) account that is part of such plan. Present law permits certain qualified transfers of excess assets from the plan assets in a defined benefit pension plan (other than a multiemployer plan) to a section 401(h) account that is part of such plan to pay for qualified current retiree health liabilities (sec. 420). Such a transfer does not affect a plan's tax-qualified status and is not a prohibited transaction (sec. 4975). Further, the assets transferred are not includible in the gross income of the employer and are not subject to the excise tax on reversions. Only one qualified transfer with respect to a plan may be made during a taxable year.

Qualified transfers must satisfy several requirements and the assets transferred must not exceed certain limits. Under one of these requirements, the accrued retirement benefits of participants (including participants who separated from service during the one-year period ending on the date of the transfer) under the pension plan must be nonforfeitable as if the plan terminated immediately before the transfer. In addition, the transferred assets (and any income thereon) are required to be used to pay qualified current retiree health liabilities (either directly or through reimbursement) for the taxable year of transfer. Transferred amounts are generally required to benefit all participants in the pension plan who are entitled upon retirement to receive retiree medical benefits (other than key employees) through the section 401(h) account. Amounts not used to pay qualified current retiree health liabilities for the taxable year of the transfer must be returned at the end of the taxable year to the general pension assets of the plan. Under a so-called maintenance of effort requirement, the employer is required to maintain current health benefit levels for a period of time after the transfer.

Only excess assets may be transferred under section 420. Excess assets are defined to be the excess of the value of plan assets (calculated as under the full funding limitation) over the greater of (1) the lesser of (a) 150 percent of current liability or (b) the accrued liability under the plan, or (2) 125 percent of current liability. For example, in the case of a plan subject to the accrued liability full funding limitation, the value of assets remaining in the plan following a transfer must be at least the greater of the plan's accrued liability or 125 percent of current liability. The calculation of excess assets is generally made as of the most recent valuation date preceding the transfer.

The provision permitting qualified transfers of excess pension assets to pay qualified current retiree health liabilities expires for taxable years beginning after December 31, 2000.

Description of Proposal

The proposal would provide an additional method under which employers could transfer excess assets from a defined benefit plan. The proposal would permit a qualified



THE DIRECTOR

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503
September 13, 1995

The Honorable Bill Archer
Chairman, Committee on Ways and Means
United States House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

It is my understanding that Congress may be asked to allow companies to take funds out of pension plans and use them to pay health benefits for active workers or for other purposes by amending Section 420 of the Internal Revenue Code. I urge you to reject such an amendment.

Section 420 now allows an employer to transfer assets tax-free from a defined benefit pension plan to a health benefits account to pay health care costs for retirees. These assets continue to be used for retirement expenses. Companies are asking that they be given these same advantages when transferring assets to pay the health care costs of active workers or to pay other employer costs.

Allowing companies to use pension assets in this manner is contrary to the most fundamental principles of the Employee Retirement Income Security Act of 1974. The transfer would not be for retirement purposes. It carries the potential for a repeat of the large pension raids of the 1980s, when over \$20 billion was taken out of plans through "asset reversions."

The proposed amendment will also increase the risk of loss to the pension insurance system. Section 420 requires that the assets remaining in the plan equal at least 125 percent of the plan's "current liability," to assure that the plan can pay benefits over time if it remains ongoing. Companies can make this calculation using actuarial assumptions that would leave a pension plan underfunded if it is terminated. Analysis shows that a transfer consistent with the proposal could nevertheless leave a plan with less than 90 percent of the funds needed for termination payments.

This is particularly disturbing in light of the December 1992 study by the General Accounting Office, "Pension Plans: Hidden Liabilities Increase Claims Against Government Insurance Programs." The GAO study demonstrates that the financial condition of plans tends to deteriorate significantly prior to their termination. A company

- 2 -

could transfer assets under the Section 420 proposal, suffer an economic reversal, and then terminate its plan with a funding level that falls well below 90 percent. A company in financial difficulty might well have an incentive to make such a transfer. Giving companies a way sharply to reduce assets in their pension plans will increase the risk of loss for plan participants and the PBGC.

Last year, on a bipartisan basis, Congress passed the Retirement Protection Act of 1994, shoring up pension funding and the PBGC. Broadening Section 420 could undermine the purpose of the Retirement Protection Act, and risks eroding confidence in our private retirement system. The Administration strongly opposes such a broadening and urges you not to include it in any legislation.

Sincerely,

A handwritten signature in dark ink, appearing to read "Alice M. Rivlin", with a stylized flourish at the end.

Alice M. Rivlin
Director

Section 13607 of the Chairman's mark is titled "Transfers of Excess Pension Assets." It should be titled "Raiding Workers Pensions."

In December 1994, Congress determined that companies should be required to make good on the pension promises they make to their workers. In September 1995, Mr. Archer proposes to allow hundreds of such companies to break those promises.

During the 1980s, over \$20 billion was taken out of workers' pension plans for general corporate use, leading to underfunded plans when the economy turned. Mr. Archer proposes to allow companies to start the process all over again. Employers would be allowed to raid pension plans "for any purpose." They wouldn't even be required to use it for their employees. And they wouldn't be required to pay an excise tax to compensate the government for the tax shelter the pension plan had provided to them all these years.

This is balancing the budget on the backs of hundreds of thousands of working men and women who are counting on their pensions. It is a shameful example of corporate welfare at its worst.