FOR AGENDA

EBAP/62/27

March 15, 1962

To: Members of the Executive Board

From: The Managing Director

Subject: Proposed Changes in the Staff Retirement Plan

The Administration Committee has recommended the adoption of the proposals contained in the attached report on the protections afforded by the Staff Retirement Plan to participants and their dependents. Similar proposals are being considered for adoption by the Bank.

The Pension Committee has considered the Administration Committee's proposals together with an affirmative report by the Chairman of the Investment Committee on the ability of the present and prospective earnings of the portfolio to sustain the additional costs which would be entailed.

With one member of the Committee reserving his position on the proposals made in paragraphs 4, 6 and 7 of the report, the Committee recommends that the Executive Board approve all the proposals made by the Administration Committee. It is recommended that if the proposals are approved by the Executive Board they be made effective as of January 1, 1962.

Formal texts of the amendments which would require to be made in the Staff Retirement Plan are being prepared in conjunction with the Bank and will be submitted at an early date.

Att: (1)

Other Distribution:
Department Heads

RP/AC/61/34

January 4, 1962

Memorandum

To: Mr. Per Jacobsson
Chairman, Pension Committee, Staff Retirement Plan

From: Phillip Thorson
Chairman, Administration Committee
Staff Retirement Plan

Subject: Proposed Changes in the Staff Retirement Plan

1. In its work with the Staff Retirement Plan, the Administration Committee has the opportunity to observe closely the significance which the protections in the Plan can have for international employees and their dependents. It reviews the elements of the Plan from time to time to see whether some of those protections might be strengthened.

In that connection, the Committee was especially interested in the comprehensive review of the UN Joint Pension Fund prepared by an eight member Group of Experts drawn from various areas of the world. They were commissioned to undertake a comprehensive review of the UN Plan, including the present and future adequacy of benefits, pursuant to a resolution of the General Assembly in 1958. Their report gave some useful perspectives for the consideration of our own Plan. The members of the Administration Committee studied what seemed to be the more important elements requiring consideration, taking into account the present rates of contributions and the available resources. In this analysis they had the advice of the Fund's Consulting Actuary and the assistance of the Investment Committee. Subsequently, they had extended discussions with their colleagues in the Bank. Those discussions resulted in recommendations on several main issues which are presented in this paper for the Pension Committee's consideration. The same proposals are being considered for adoption on the Bank side.

2. The Administration Committee recommends that the Staff Retirement Plan should be improved in the following ways:

(a) the pension benefits for persons retiring from the Fund should be improved by increasing the benefit rate and the maximum pension limit;

(b) the pension protections for disabled persons, widows and qualified widowers should be strengthened; and

(c) the protections provided for children should be increased.

INCREASE IN RETIREMENT PENSION BENEFITS

3. The UN Group of Experts concluded that the major problem in the UN Plan stemmed from the fact that pensions were based, as in the Fund, on net rather than gross salaries. The consequence of using net pay for computing pension benefits was that the resulting pensions ran substantially lower than those based on comparable gross salaries in outside employment. The difference was shown to be particularly marked at higher salary levels because the graduation of income taxes creates a widening gap between net and gross rates of pay as salaries rise. In addition, the pensions themselves when actually received would not be exempt from income taxes.

The Expert Group devoted a great deal of attention to the net-gross problem and considered different alternatives for dealing with it. The conclusion reached was that, as a matter of principle, a gross-salary base should be adopted as an equitable level of pensionable remuneration if UN conditions were to be made truly comparable with those outside the organization. Such a recommendation had a certain relevance at UN because its official salary scale is, in fact, stated in terms of gross salaries (that is, salaries before deduction of the Staff Assessment Tax).1/ However, the Experts found a number of practical difficulties in going to a full-gross system, and in the circumstances they recommended that the notional "salary for pension purposes should be the mid-point between the net and gross on the UN scale.2/ Consequently, both contributions and benefits would be based on a "half-gross" level of pensionable remuneration. This recommendation was adopted by the General Assembly.

4. In considering the same problem, our own Committee also considered various methods of dealing with it. The Committee noted that in the Fund the improvement in the rate of benefit from 2 per cent to 2 1/2 per cent for each of the first 10 years of service adopted in 1959 had already achieved a similar result for pension benefits of persons who serve no more than that length of time. Therefore, the Committee believed it would be preferable to continue in the same direction and extend the higher

1/ For example, at UN gross salaries of $6,800, $10,800, $17,000, $21,400 and $27,000 correspond to net salaries of $5,600, $8,500, $12,500, $15,000 and $18,000, respectively.

2/ In addition, the level of pensionable remuneration for professional and higher categories is to be adjusted (upwards or downwards) when the weightedaverage of post adjustments changes by 5 per cent, measured from January 1, 1962.

rate of benefit to a longer service period than to venture into a new pattern of calculations based on a new concept of "half-gross" salaries. The Committee felt that such an extension had practical importance inasmuch as nearly one half of the present participants in the Retirement Plan have now had over 10 years of service, and some will soon have 16. Hence, the Committee proposes that the 2 1/2 per cent benefit rate be extended for a further 15 years of eligible service, thus making that better rate applicable in respect of each of the first 25 years of eligible service. The Committee would hope that the future experience of the Plan would later justify extending the 2 1/2 per cent rate to additional years of service.

5. The effect of the new rate and comparisons with the UN scheme[1] are presented in the table below:

	Average Net Salaries				
	$5,600	$8,500	$12,500	$18,000	$25,000
Pensions After:					
20 years					
Fund (Present)	$2,520	$3,825	$5,625	$8,100	$11,250
Fund (Proposed at age 65)	2,800	4,250	6,250	9,000	12,500
Fund (at age 60)	1,960	2,975	4,375	6,300	8,750
U.N.	2,255	3,505	5,364	8,218	12,036
25 years					
Fund (Present)	3,080	4,675	6,875	9,900	13,750
Fund (Proposed at age 65)	3,500	5,313	7,813	11,250	15,625
Fund (at age 60)	2,450	3,719	5,469	7,875	10,937
U.N.	2,818	4,382	6,705	10,273	15,046
30 years					
Fund (Present)	3,640	5,525	8,125	11,700	16,250
Fund (Proposed at age 65)	4,060	6,163	9,063	13,050	18,125
Fund (at age 60)	2,842	4,314	6,344	9,135	12,687
U.N.	3,382	5,258	8,045	12,327	18,054

1/ It should be noted that in the U.N. the normal retirement age is 60.

6. It is proposed that this new rate should apply both to present and future contributing participants and also to the participants who have already retired or who hereafter retire on normal, early immediate or early deferred pensions, but without retroactive adjustment of previous payments.

7. Section 4.1(b) provides that the maximum pension should not exceed 72 per cent of the highest average remuneration. The Committee proposes that in the light of the foregoing recommendations, the maximum pension limit be increased to 75 per cent.

INCREASE IN DISABILITY AND WIDOW'S PENSIONS

8. Under our Retirement Plan a person retired for disability reasons is entitled to a pension of at least one third of his highest average remuneration. (This minimum applies except for a person who began his service after the age of 48 1/3 years; in such a case, the disability pension could not exceed what his retirement pension would have been had he served to age 65.) If the disabled person has served more than 16 2/3 years, his disability pension would be greater than one third of his highest average remuneration, the calculation being based on the number of his years of service times 2 per cent times his highest average remuneration.

The Committee believes that henceforth disability pensions should be based on the same percentage factor (namely, 2 1/2 per cent for the first 25 years of service) as is proposed for normal pensions. When the 2 1/2 per cent factor for the first 10 years of service was adopted in 1959, the Committee wanted to apply it to disability pensions but it could not be afforded within the financing available then. However, it could be afforded now. The consequences of such a change would be that:

(a) the disability pension of a person with long service would be the same as a normal pension for the same period of service;

(b) the disability pension would start to move above the one-third minimum after fewer years of service (13 1/3 years as against 16 2/3); and

(c) persons who begin service up to age 51 2/3 years would still be eligible for the minimum disability pension.

9. If a participant dies in service, his widow or dependent widower is entitled to a pension equal to one half of what his disability pension would have been at the time. Under the foregoing proposal

to improve the factor for disability pensions, the widow's pension would automatically increase too in certain cases. However, the pension for a widow entitled to one half of the minimum disability pension would still amount to only one sixth of the participant's highest average remuneration. The Committee believes that such a pension would be inadequate in most cases. The Committee, therefore, recommends that the minimum pension for a widow or dependent widower of a participant who dies in service be 25 per cent of his highest average remuneration. This would be subject to the proviso that the amount could, in any case, not exceed the amount of the disability pension to which the principal would have been entitled at the time of his death. The Committee recommends also that if a person drawing a disability pension should die, the widow or dependent widower should be entitled to the same minimum pension.

10. The Committee also recommends that the improvements in disability and widow's pensions should apply to pensions which became effective since April 17, 1959, but without retroactive adjustment of pension payments.

IMPROVEMENT IN THE CHILDREN'S BENEFIT

11. The present children's benefit is paid in respect of children up to the age of 19 at the rate of $300 for a child with a surviving parent, or $600 for a full orphan. These provisions were modeled after the initial UN Pension Fund regulations. With the passage of time, the fixed sums have become less and less adequate. Likewise, the benefit would not cover some cases where a need is likely to exist.

12. Following the report of the UN Expert Group, the UN Pension regulations were recently liberalized in both respects. The Committee believes that the Fund should similarly change its provisions. One change would be to broaden the coverage of the benefit as follows:

(a) the benefit should be extended to age 21 for children who are in full-time attendance at school;

(b) the benefit should be paid also for eligible children of retired participants who retired on normal or disability pensions or on early pensions after 10 years of eligible service and have reached normal retirement date;

(c) however, no benefit would be paid to a child who is married.

13. The Committee also proposes that children's benefit should be a proportion of the basic retirement or disability benefit of the participant, subject to upper and lower limits. In such a way the

children's benefit will be related to some extent to the salary level and the length of service of the participant. The benefit payable would be computed as follows:

(a) if there is a living parent, the annual benefit payable to each child would be one third of the participant's basic benefit (i.e., the disability or retirement pension for which the participant was eligible at the time he died), subject to a minimum of $300 and a maximum of $600 per child. However, the total amount payable with respect to all eligible children could not exceed the smaller of:

(i) $1,800 per annum divided equally among all such children, or

(ii) an amount per annum which when added to any retirement benefit or widow's benefit then payable would equal the highest average remuneration of the participant, with such amount equally divided among all such children.

(b) If there is no living parent, the benefit payable to each child would first be computed as in (a) above, and

(i) where there is only one eligible child, he would also receive an additional annual benefit equal to the greater of $300 or 25 per cent of the participant's basic benefit

(ii) when there are two or more eligible children, they would also receive the greater of $600 or 50 per cent of the basic benefit, and such total additional benefit would then be divided equally among them.

CHANGE IN RATE OF REGULAR INTEREST

14. Section 7.1(f) of the Staff Retirement Plan provides "it (the Pension Committee) shall establish from time to time the rate of regular interest to be compounded annually as determined by the Administration Committee. It shall be used in all actuarial calculations required in connection with the Plan." The original interest rate of 2 1/2 per cent was changed effective May 1, 1956, to 3 per cent. According to the recent actuarial valuation, the rate of earnings required to provide regular benefits under the Plan, including the proposed new benefits, would be 3 1/2 per cent. The general trend in recent years has been toward the adoption of a 3 1/2 per cent interest rate for pension plans, and the Consulting Actuary would concur in this rate for the Fund Plan. For the fiscal year ended April 30, 1961, the yield on the amount originally invested, the basis upon which the

actuarial valuation of the Plan is made, amounted to 4.43 per cent. For some years, the realized rate of return has exceeded 4 per cent in each year. The Investment Committee has been consulted and agrees that the 3 1/2 per cent interest rate would be entirely safe. Accordingly, the Committee recommends that the Pension Committee change the rate of regular interest to be used in all calculations in connection with the Plan for periods commencing on or after January 1, 1962, from 3 per cent per annum to 3 1/2 per cent per annum, and amend the interest resolutions accordingly.

FINANCIAL IMPLICATIONS

15. The present rate of contribution is 14 per cent for the Fund and 7 per cent for participants. The Consulting Actuary has made several calculations to indicate the cost implications of various alternative amendments which were considered. It appears that, if the interest rate is changed to 3 1/2 per cent per annum and the surplus of $130,000 shown on the last actuarial balance sheet is absorbed, the proposals set forth in this paper will not entail payments for present active participants and present retired participants over and above the present rates of contribution. With regard to the future, the rates will depend on the distribution of sex and age of future participants and, of course, on the actual over-all experience of the Pension Fund.

TRANSFER OF PENSION RIGHTS BETWEEN THE FUND AND THE BANK

16. The Staff Retirement Plan presently permits the transfer of pension rights in the case of transfer of personnel between the Fund and the Bank. This provision requires an actuarial valuation for each case to show the amount one Plan shall transfer to the other. After this provision was put into the Plan, the Fund and Bank worked out a similar arrangement with the United Nations for transfer of pension rights which utilizes a simplified method of calculating the amount of funds to be transferred in each case. The Committee recommends that the Plan be amended by deleting the present provision relating to the Bank and that the provisions applying to UN transfers be extended reciprocally to the Bank.

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17. If the Pension Committee agrees in principle to the changes recommended by the Administration Committee, the proposals could be forwarded to the Executive Board for approval. The formal text of the amendments are being prepared in conjunction with the Bank and will be submitted at a later date.