The Evolution of Entitlement: Retirement Income and the Problem of Integrating Private Pensions and Social Security

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THE EVOLUTION OF ENTITLEMENT:
RETIREMENT INCOME AND THE
PROBLEM OF INTEGRATING PRIVATE
PENSIONS AND SOCIAL SECURITY

Patricia E. Dilley*

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Pension benefits given to low-paid employees as an abstraction are taken away in the fine print of the income tax code.

—Senator Gaylord Nelson

I'm old, I'm helpless and feeble . . . and the days of my youth have gone by . . . and it's over the hill to the poorhouse . . . I must wander alone there to die . . .

I. INTRODUCTION

Entitlement is the public policy hot button of the mid-1990s. The drive to "restrain the growth of entitlements" has taken a central role in the budget battles facing Congress each year. In the context of public debate over federal spending, even the word "entitlement" has taken on unsavory connotations of getting something for nothing, of rewards based on status rather than merit.

Nowhere does the issue of public spending on "entitlements" loom larger than in the area of programs providing retirement income security. Such programs include Social Security, Old Age Survivors' and Disability Insurance (OASI), government and veterans' pensions, and Supplemental Security Income (SSI) aid to the poor elderly. These programs are perhaps the largest pub-


2. L. Flatt & W. Lilly, Over the Hill to the Poorhouse, on Hard Travelin' (Columbia Records 1963). This song version of a poem was recorded in the 1930s and later by Southern bluegrass artists, including Flatt and Scruggs. The song tells the story of an old man whose three children threw him off the farm and forced him to wander the roads in poverty. See id.


8. See 42 U.S.C. §§ 1381-1383(c). I do not address the separate issue of health
lic spending programs under which every beneficiary meeting initial eligibility criteria must receive the benefit promised under the law, regardless of the state of the federal exchequer. Public calls for restraining the growth of these entitlements are now a standard part of every pundit's analysis of the federal deficit.

Yet entitlement to future income is fundamental to the phenomenon of retirement. The dilemma of old age is how to afford to live until death. As life spans lengthen and the prospect of living to Shakespeare's seventh age of "mere oblivion" becomes more real, how do we ensure that we will have adequate shelter, food, and care to the end of life beyond the time we are able to provide for ourselves through work? The fear of outliving one's accumulation of resources for assuring income, paired with the fear of loss of control over the daily circumstances of life, are the curses of old age at the end of the twentieth century. The blessing of long life, as it becomes more the norm than the exception, carries with it the threat of loss of autonomy and control.

Without a legally enforceable expectation of a predictable level of income—whether from private pensions, savings, or Social Security—until death, no worker could be expected to leave the work force voluntarily, which after all is the essence of the twentieth century concept of retirement. Expectations of a stable in-

care for the elderly provided through Medicare, Medicaid, and employer-provided retiree health insurance.

9. See id. §§ 401-403, 1381-1383(c).

10. This definition of public spending entitlement leaves aside the category of tax expenditures, such as home mortgage interest deductions and failure to tax the earnings of qualified pension plans. They are not included in the discussion here, as they are not popularly understood as entitlements by many involved in the budget debates.

11. WILLIAM SHAKESPEARE, AS YOU LIKE IT act 2, sc. 7, l. 165 (Alan Brissenden ed., Oxford Univ. Press 1993) (1564). See generally the speech of Jaques: All the world's a stage, . . .

And one man in his time plays many parts,

His acts being seven ages . . . .

Last scene of all,

That ends this strange, eventful history,

Is second childishness and mere oblivion . . . .

Id. at ll. 139, 142-43, 163-65.

12. Defining "retirement" is a problematic venture. See, e.g., Buffalo Bills, Inc. v. United States, 31 Fed. Cl. 794, 802-03 (1994) (competing definitions of "retirement" from Oxford English Dictionary and Webster's Third New International Dictionary offered by petitioner and respondent). I follow in this Article the current thinking in historical analysis that distinguishes between retirement as a voluntary cessation of work at a specific age as opposed to cessation of work because of disability. See WILLIAM GRAEBNER, A HISTORY OF RETIREMENT 11-17 (1980); discussion
come are important at most stages of a working life, but older workers with fewer options and more immediate fears of the loss of ability to work are likely to place far more importance on enforcement of such expectations. In a very real sense, the debate over entitlements for the elderly is a debate over retirement itself.

There are clear distinctions between the legal relationships creating private pension entitlement and Social Security benefit entitlement. Nonetheless, an analysis of the function and context of retirement income rights reveals that the presumed gulf between public and private rights in this area is not nearly so wide as it may at first seem. In this Article I examine the historical roots and evolution of the American system of entitlement to old-age income security in order to understand why in one technical area—the integration of private pension plans with Social Security—workers' presumed entitlement to private pensions is less secure than their entitlement to Social Security.

My starting point is a seemingly straightforward question: Why does the primary direct statutory link between Social Security and private pensions—pension integration—result in lower private pension benefits for the portion of the worker population, low-wage workers, that the 1935 Social Security Act was expressly designed to benefit? To answer that question, it is necessary to go far beyond the technical structure of the pension nondiscrimination rules, and examine the historical and political evolution of old-age entitlements and the modern institution of voluntary old-age retirement. The peculiarly prospective character of retirement entitlements is the key to discovering a consistent set of principles upon which an appropriate relationship between public and private retirement benefits can be based.\(^{13}\)

\section*{A. Conflict of Integration and Entitlement Principles}

Pension integration is the only major area in which the public entitlement represented by Social Security retirement benefits and the private entitlement represented by private pension plans are

\footnote{\textit{infra} Part III.\[^{13}\] This Article focuses on voluntary retirement, as opposed to cessation of work because of disability, although in practice it is sometimes difficult to wholly distinguish the two. See \textsc{Deborah A. Stone}, \textsc{The Disabled State} (1984) for an excellent discussion of disability entitlements and the difficult judgments involved. See also Matthew Diller, \textsc{Entitlement and Exclusions: The Role of Disability in the Social Welfare System}, 44 \textsc{UCLA L. Rev.} 361 (1996) (discussing disability benefits under social insurance and public assistance paradigms).}
Integration of private pension plans with Social Security essentially allows an employer to pay lower proportionate pension benefits to low-wage workers than to high-wage workers, based on the size of the lower-paid worker’s Social Security benefit or payroll taxes paid. This kind of disparity is generally forbidden under the pension “nondiscrimination” rules, which are intended to withhold favorable tax treatment from pension plans that provide better pension coverage for high-paid than for low-paid workers. The integration rules are a statutory exception to these nondiscrimination requirements.

Pension advocates and analysts have criticized integration since its inception in 1942 as an assault on the retirement benefits of lower-paid workers. Most critiques focus on the results rather than on the principles of integration, and have suggested limiting, but not eliminating, its role in reducing retirement income for low-wage workers. But if the analysis begins instead with the nature of the right to the Social Security benefit—including the redistributive design of the benefit structure—a more compelling critique of integration emerges, unrelated to questions of whether some standard of adequacy could be met by an integrated plan.

I argue here that pension integration violates both public and

17. See id. § 401(a)(5).
19. See discussion infra Parts VI-VII.
private entitlement rights that are a necessary precondition to retirement. Integration effectively voids the basic public entitlement principles of prospective redistribution, assured income regardless of need, and individual opportunity to acquire—principles that are grounded in almost two centuries of public pension history and reflect essential elements of economic and political democracy.\(^{20}\) Integration also violates the private pension entitlement because it reduces private pension benefits for low-wage employees who would otherwise receive those benefits in addition to their Social Security benefits. Because integration at its core cannot be reconciled with either public or private entitlement principles, attempts made in the 1986 Tax Reform Act\(^{21}\) to rationalize the integration rules and mitigate their effects on low-income workers could inevitably have only a marginal impact.

The pension integration rules are a technical response to a larger policy dilemma: reconciling the roles of public and private entitlements in ensuring mass retirement. The implications of the practice of integration, and of the violation of pension rights it represents, reach beyond the technical parameters of the complex and abstruse tax qualification rules that govern pension plans. The persistence of integration in the face of forty years of attempts to eliminate it\(^{22}\) is based on a critical misunderstanding of the role and structure of Social Security, and reveals a fundamentally manipulative approach on the part of policymakers to the problem of retirement income security for low-wage workers. Examining integration is one way to begin to make sense of the larger issues of whether an aging society can adequately maintain the institution of mass retirement in the context of liberal democratic capitalism.

**B. Integration as a Microcosm**

The focus of this Article is on the development of the retirement entitlement principle and the ways in which the rationale and mechanisms of pension integration, from its inception in the early 1940s up to the 1986 Tax Reform Act, contradict that principle; the revision of the integration rules in the 1986 Act, including the rationale for, reaction to, and effects of those changes; and finally, on alternative models of retirement income security in the absence

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20. See discussion infra Part VII.
22. See discussion infra Part VI.
or presence of integration.

Part II explores the theoretical debate over public income entitlements, and suggests that the function of the entitlement concept may be quite different in the retirement setting than in the general antipoverty context. The American approach to earnings-based retirement entitlement is based on a deeply held popular, democratic capitalist ideology of market opportunity and economic mobility. Income-targeted entitlements are politically insupportable, seen by the public and politicians as undemocratic, intrusive, and destructive of individual responsibility and self-reliance. In contrast, earnings-based entitlements are more widely supported, and are seen as consistent with American self-images of worth based on effort and opportunity to accumulate. Any provision that imposes income targets on the earnings-based


24. See Marmor et al., supra note 3, at 4-16 (noting that American social welfare policy seems to be in conflict with our idea of the "good or legitimate" state). The belief that poverty is the fault of the poor themselves, and that benefits based on need promote further dependency, has a long history. For example, Benjamin Franklin forthrightly expressed his strong belief in individual effort and economy as the answer to poverty at any age, including extreme old age. See Howell V. Williams, Benjamin Franklin and the Poor Laws, 18 Soc. Serv. Rev. 77 (1994) (discussing Franklin's opposition to any provision, public or private, for the poor). Franklin was steadfastly opposed to English Poor Laws that required local governments to provide some aid to the poor as well as to private charity provision of poor relief. See id. at 77. In a 1773 letter Franklin expressed the view that English laborers "lacked industry and thrift," whereas German workers had both:

When I consider that the English are the offspring of the Germans, . . . when I see nothing in nature that should create this difference . . . I have sometimes doubted whether the laws peculiar to England, which compel the rich to maintain the poor, have not given the latter a dependence, that very much lessens the care of providing against the wants of old age.

Id. (emphasis in original).

Franklin's preferred approach to old-age security was the establishment of private old-age homes, financed by fixed entry fees and run by private volunteers. Id. at 81. Franklin wrote in 1772 to an English baron who advocated aid to the poor that these old-age homes seem calculated to prevent poverty, which is rather a better thing than relieving it; for it keeps always in the public eye a state of comfort and repose, with freedom from care in old age, held forth as an encouragement to so much industry and frugality in youth as may at least serve to raise the required sum [for entry to the old-age home].

Id. (emphasis in original).

25. See discussion infra Parts III-IV.
entitlement—as integration effectively does—is fundamentally inconsistent with the function and purpose of the entitlement.

Part III provides an overview and analysis of the origins of this earnings-based entitlement structure in American responses to poverty, old age, and war. The centrality of both redistribution and the earned right concept to Social Security's structure and purpose cannot be understood outside the historical context of the modern innovation of retirement and the American approach to poverty in old age that developed out of local poor relief and veterans' pension systems. The existence of the Civil War pension system, which provided benefits for a substantial percentage of the elderly up to the 1920s, served as direct precedent for Social Security and prepared the way for a broad service-based, old-age benefit of which the purpose was to prevent rather than ameliorate poverty.

Part IV explores the dual models of private insurance and pensions on one hand, and public social entitlements on the other, that developed simultaneously in the post-Civil War era. As discussed more fully below, the enactment of Social Security in 1935 was the culmination of a long period of agitation for "industrial welfare" and social reform, and was an important element in anti-poverty efforts in the wake of the Great Depression. However, the central function and basis of the redistributive features of Social Security were misinterpreted by employers and pension analysts. The contributory financing structure of Social Security was taken as the literal basis for entitlement by pension analysts, while employers viewed the program as a way of relieving the private sector from the burden of providing retirement pensions for low-wage workers. This fundamental misapprehension of the source and nature of the Social Security entitlement provided the theoretical basis for allowing employers to eliminate or reduce private pension coverage for their low-wage employees through integration.

Part V focuses on the development of the nondiscrimination rules for employer-provided pensions and integration as the exception to those rules, from the early 1920s through the Revenue

26. See discussion infra Part III.A.
27. See discussion infra Part III.
28. See discussion infra Part IV.
29. See discussion infra Part IV.
30. See discussion infra Part IV.
Act of 1942, which codified integration. Employers, Congress, and the IRS, from at least the 1942 Revenue Act forward, used the integration rules as a means of ensuring that workers would receive no more than what the employer and the government deemed to be adequate replacement of pre-retirement wages from the combination of Social Security and pension benefits through reduction in the private benefit. The results of integration are thus quite contrary to the popular conception of Social Security as providing a basic tier of income to which private pensions would be added. Because employers viewed Social Security as a government-provided pension plan for low-wage workers, integration appeared to be a logical necessity, even though it effectively eviscerates the redistributive element of the Social Security benefit structure through elimination or reduction of low-wage workers' private entitlement to pension benefits.

Part VI analyzes various attempts to eliminate or reform integration through revisions to the integration rules made by the 1986 Tax Reform Act. Section 401(l) of the Internal Revenue Code was enacted in the 1986 Tax Reform Act to codify a new approach to pension integration. Nonetheless, because it was based on a fundamentally flawed understanding of the Social Security entitlement principle, the effort at reform was doomed to failure.

Part VII discusses the standard critiques of integration, its continued acceptance as a necessary part of the employer-provided pension system, and the fundamentally flawed view of retirement entitlements that both critics and supporters of integration share. In light of the more compelling critique of integration that emerges from the earnings-based entitlement perspective,

32. Id.
33. See discussion infra Parts V, V.I.C.
34. See ROBERT J. MYERS, SOCIAL SECURITY 12 (4th ed. 1993) ("The real reason for having a social security system in addition to private insurance coverage is not primarily that of cost, but rather that social benefits on a social adequacy basis can only in this way be provided to a large sector of the population.").
35. See discussion infra Part IV.B-C; see also COLIN GORDON, NEW DEALS: BUSINESS, LABOR, AND POLITICS IN AMERICA, 1920-1935, at 275-76 (1994) [hereinafter GORDON, BUSINESS, LABOR, AND POLITICS] (noting that business support was far from uniform).
36. See discussion infra Part V.
38. See discussion infra Part V.I.D.
I suggest a new approach to retirement income security without pension integration that is perhaps more consistent with the real purpose and current reality of both the private pension and Social Security systems.

II. RETIREMENT ENTITLEMENTS: FROM PRACTICE TO THEORY

The seemingly technical question of whether pension integration is a necessary or consistent element of the American retirement income security system cannot be answered without addressing the larger questions of the function and basis of private and public income entitlements that make retirement possible. Pension integration, as described more fully in Part V, is based on the premise that employers should be allowed to reduce private pensions for their low-wage employees because Social Security benefits replace a higher portion of low-wage salaries than of high-wage salaries, in essence treating the Social Security benefit as part of the employer’s compensation package. The practice of integration is a logical extension of a particular view of the source and function of Social Security benefits: that Social Security is simply part of the employer-provided pension system.

Critiques of integration have generally focused on its economic consequences in reducing ultimate retirement income for affected low-wage workers. However, such critiques, as discussed below, cannot wholly counter the argument that integration in some form is necessary to prevent “overpensioning”—retirement income from the combination of Social Security and private pensions that might exceed pre-retirement earnings, a result that is assumed to be undesirable from a public policy perspective.

I begin here, in contrast, with origins rather than consequences. This Article presents an examination of the genesis and evolution of fundamental principles of non-needs-based entitlement, in an attempt to determine whether the practice of integration, regardless of results, is intrinsically incompatible with the earnings-based entitlement character of the American retirement system. That question, in turn, cannot be adequately answered without considering whether public income entitlements that are

39. See SCHULZ & LEAVITT, supra note 14, at 1, 7-19 (discussing the mechanics of the integration process).
40. See discussion infra Part VII.
41. See discussion infra Part VI.C-D.
42. See discussion infra Part VI.C.
not based on need are a necessary element of retirement income security. After all, if a completely needs-based public system complemented with an earnings-based private system would provide a better basis for mass retirement, it would hardly matter that integration might be in conflict with earned-entitlement principles.

While theoretically such a two-tier system could be developed and implemented, the historical development of old-age assistance programs in America, as well as Europe and Canada, shows that the earned-entitlement principle combined with public redistributive benefit programs were the necessary preconditions to the practice of retirement as it has developed in the mid-to-late twentieth century. Earnings-based entitlement is not only consistent with economic individualism, it is the essential expression of individual economic rights in the American capitalist context.

The American retirement income system, with its mixture of public and private entitlements that are primarily based on work, is grounded in the distinction between the right to opportunity, which is an essential element of liberal capitalist notions of democracy, and a status-based right to income, which historically has been seen by Americans as antithetical to an opportunity-based society. Pension integration essentially imposes an indirect needs test on the private pension entitlement by limiting the possible combination of private and public benefits to an amount less than the individual's pre-retirement earnings. Thus, pension integration, when examined in the historical context of the development of modern retirement, is in conflict with fundamental retirement principles. The question then becomes whether preventing "overpensioning" is so important a goal that it justifies maintaining integration regardless of the principled conflict. As discussed in Part VI, I suggest the answer to that question is no.

43. See discussion infra Parts III-IV.
44. See generally JOHN LOCKE, TWO TREATISES OF GOVERNMENT 353 (Peter Laslett ed., Cambridge Univ. Press 1988) (1690) (noting that in taking part in society "no rational Creature can be supposed to change his condition with an intention to be worse"); JOHN RAWLS, A THEORY OF JUSTICE (1971) (setting forth principles of justice that place free and rational persons in a position of equality).
45. For more examples of American attitudes toward welfare and the "right" to income see KATZ, supra note 23, at 251-91, and Joel F. Handler, "Constructing the Political Spectacle": The Interpretation of Entitlements, Legalization, and Obligations in Social Welfare History, 56 BROOK. L. REV. 899 (1990).
47. See id. at 28-29.
Before examining the historical roots of retirement entitlements, it is necessary to establish a framework within which the essential elements of the retirement income system—entitlement, worthiness, retirement, and redistribution of income—can be understood as concepts that have developed in a particular historical context. The relationship between legal and economic entitlement in general is too complex to be fully explored in this Article. Nonetheless, I want to suggest some perspectives from which to at least begin to answer the question of whether public entitlements have, in fact, any noneconomic theoretical basis that would pose a challenge to the practice of pension integration.

A. Entitlement as the Precondition of Retirement

The concept of entitlement has been described as the transformation of a mere private interest into one that society in general will give legal force against challenge or interference from the interests of others. Much of the legal analysis of entitlement has been concerned with exploring the internal structure of the legal entitlement and determining different forms and types of entitlement. Since Wesley Newcomb Hohfeld’s initial elucidation of the entitlement concept early in this century, scholars have grappled with identifying and categorizing the building blocks or essential elements of the various types of entitlements. These types are generally separated into either legal, moral, and public entitlements, or property, liability, and inalienability entitlements.

I propose to narrow the analysis of entitlements in the context of pension integration from the relatively abstract discussion of the legal framework and extent of entitlements in general to the age-

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Because any interest to which we would like to give legal force is liable to come into conflict with other interests to which we would also like to give legal force, entitlements must be... constructed so that they do more than simply “give legal force” to certain interests. They must also specify the extent and type of legal force that a given interest has in any particular context and in relation to any other particular entitlement.

Id. at 823.

49. See Wesley Newcomb Hohfeld, Some Fundamental Legal Conceptions as Applied in Judicial Reasoning, 23 YALE L.J. 16 (1913).

specific context of old-age entitlements and the problem they address—the modern institution of voluntary retirement in extended old age. By focusing on the purpose and historic roots of this specific type of economic entitlement, I hope to reach some conclusions about the appropriate relationship between public and private retirement systems and shed some light on why public and private entitlement, which make retirement possible for most workers, evolved as earnings-based, rather than needs-based or citizenship-based rights.

The debates over the concept of public entitlement rights were given a theoretical legal context with the publication in 1964 of Charles Reich's classic article, *The New Property*. Reich suggested that the web of antipoverty programs that were established in the New Deal created a new property right, an "entitlement" in welfare benefits, that would give recipients a sort of property right in those benefits. The "new property" entitlement would formalize the relationship between government and recipients, to protect recipients from arbitrary decisions and manipulation by government decision makers, while maintaining the antipoverty, redistributive purpose of welfare programs.

The new property right in welfare benefits has frequently been contrasted with rights to Social Security entitlements, which are portrayed as contractual rather than propietal in character. The contract between worker and government was presumably based on the contributory financing and earnings-based benefit structure that was described from the inception of Social Security in the 1930s as an "earned right," assuring payment of benefits. The public perception that some sort of legal right must vest in Social Security benefits persists despite the Supreme Court's decision in *Flemming v. Nestor* that Social Security benefits are neither property nor contract rights, and may be altered or denied by Congress so long as its action is not "utterly lacking in rational justification."

I suggest that this public perception is based on more than

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52. See id. at 733.
53. See id.
55. See id. at 1448-54.
57. Id. at 611.
simple self-interest. The proposition I wish to explore is whether the institution of voluntary retirement, in an American context infused with strongly held beliefs in the possibility of individual opportunity and mobility, virtually required the development of an earnings-based entitlement right that is inconsistent with income targeting, of which integration is a specific technical example. Prospectivity may be the essence of the classical notion of individual entitlements and the basis of a legal system designed to maximize individual independence and autonomy.\textsuperscript{58} In the retirement context, I suggest that the substance of the entitlement is wholly prospective in that it consists entirely of a right to future consumption that can only be exercised long after it has been established. In other words, the right to any retirement entitlement, whether a private pension, a retirement savings account such as an individual retirement account (IRA),\textsuperscript{59} or the "right" to a Social Security benefit, represents the right to future rather than current consumption, a right the fulfillment of which depends on the productivity of society as a whole at the time of consumption.

Since a voluntary decision to retire is largely based on the assurance of future income from such prospective entitlements, the circumstances of securing and enforcing the right—in essence, the legal bases for the economic right—are of extreme importance to the prospective retiree. It is the need to assure access to prospective consumption after a working life has ended and retirement has begun that has shaped the development of both public and private retirement entitlements and in which the very concept of entitlement is rooted.\textsuperscript{60}

\textbf{B. Entitlement for the Worthy}

Much of the analysis of earnings-based benefits such as Social Security has centered on contrasting the relatively high status and political security of earnings-based entitlement programs with the low status and lack of political security of poverty-based programs.\textsuperscript{61} Many analysts suggest that the preference given to earn-

\begin{thebibliography}{9}
\bibitem{58} See Simon, supra note 54, at 1433-35.
\bibitem{60} See discussion infra Part III.
\bibitem{61} See, e.g., Gordon, Pitted But Not Entitled, supra note 23, at 4-6; see also Handler, supra note 45, at 905 (giving an example of Aid to Families with Dependent Children (AFDC) as a program that illustrates not only patriarchy and race but also the importance of the deviant status of poor mothers in the paid labor force).
\end{thebibliography}
ings-based programs and the rejection of needs-testing for such benefits is a product of progressive and New Deal era liberal ideology that created the illusion of contract in contributory social insurance.  

However, as discussed in Parts III and IV, the fear of and cultural revulsion against dependency in old age, and the establishment of public old-age entitlements based on peculiarly American assumptions concerning individual economic opportunity and mobility and rights to accumulate wealth, long predated the Progressive Era and the New Deal. The development of old-age income support programs, from the English Poor Laws to Civil War pensions to Social Security, suggests that American earnings-based old-age entitlements have evolved over the last 200 years for almost the same purpose proposed for the new property right by Reich—to protect those elderly viewed as "worthy" of such entitlement from control and degrading treatment by those dispensing poor relief.

American public and political approaches to the problem of income support for the poor, the disabled, and the elderly rest on expectations about work and opportunity, and on the assumption that work is available for those who wish to work and have no acceptable reason for not doing so. The development of American old-age entitlements was based on the premise that rights belong to the worthy and that certain conditions create a presumption of need that should trigger the exercise of those rights in the form of benefits.

The importance of the ideology of opportunity and access to economic mobility in the institutional structure of American public aid programs has perhaps been insufficiently considered in critiques of poverty and social insurance programs. Yet the history of provisions for the elderly clearly reveals an important link between entitlement, earnings and worthiness, and assumed economic opportunity that has shaped the nature of rights to benefits and expectations of retirement.


63. See discussion infra Part III.A.

64. See discussion infra Part III.B.

65. See discussion infra Parts III-IV.

66. See Handler, supra note 45, at 902-04.

67. See discussion infra Part III.

68. See discussion infra Part III (discussing the link between "worthiness" and public aid); see also KATZ, supra note 23, at 13-14 (discussing the impact of social
C. Mass Retirement and Earned Entitlement

Earnings-based entitlement programs are held in generally low esteem by policy analysts concerned with adequate income provision for the poor: entitlements are sloppy, they defy top-down assessments of need and decisions to induce pay, and they are not efficient since redistributed funds may end up going to someone who does not need them at the time of receipt. Yet the very factors that give rise to these critical assessments of entitlements appear to be essential to induce workers to engage in life-long productivity and then to retire at sixty-five, even if physically and mentally capable of continued work.

The old-age entitlement can be distinguished from the general poverty entitlement because of the condition it addresses—old age and the presumed loss of the ability and opportunity to earn. While those who lived long enough to become truly unable to work have historically been entitled to aid, no expectation of a life lasting for a substantial period beyond work existed for most workers until the twentieth century. The disappearance of the expectation of work for the elderly occurred simultaneously with the changes industrialization made in the nature of work itself, increasing the risks of dependency because of economic downturns and creating the perceived need to control and rationalize the labor force.

I suggest, based on a survey of the historical literature concerning the development of the retirement phenomenon, that the need for mass retirement made necessary earnings-based income entitlements that preserve the opportunity to accumulate. The prospect of opportunity to accumulate income and assets as needed or desired, without the penalty of losing benefits through means-testing, is implicit in the principle of entitlement, and is essential precisely because of the prospective nature of old-age entitlements.

Social Security benefits represent a claim on society in general, rather than on a specific employer, on the grounds of age and prior service to the society and economy through work. Entitlement to public benefits in the American tradition has always been precedents in shaping early America's poor relief); Handler, supra note 45, at 906-09 (emphasizing the plight of poor mothers as a mechanism for understanding welfare).

69. See, e.g., Steuerle & Bakija, supra note 15, at 1764.
70. See discussion infra Part IV.
71. See discussion infra Parts III-IV.
based on a judgment of moral worth resulting from service to the country or other evidence of good character. The innovation of the Social Security system was to broaden the criteria for entitlement from military service to work in general. In this sense, the term "earned right" is an accurate description of the relationship between beneficiaries and benefits.

The public entitlement, the earned right from this perspective, is the right to the whole benefit to which the worker may add, if fortunate enough, private rights to pensions and savings. In contrast, integration is based on the notion of an "appropriate" replacement rate, a targeted income level in retirement that sets a ceiling on what workers should be allowed to accumulate under the private pension. In effect, integration grafts an income-based target onto the earnings-based entitlement that is inconsistent with its fundamental structure and purpose.

D. Metaphor and Reality of Contributory Entitlements

In the pre-World War II period, American employers established pension programs primarily to ward off union organization; to encourage unproductive older workers to make way for younger workers, while promoting employment longevity for valued workers; and to accumulate capital while reducing payroll outlays. In this context employers came to view Social Security as a federally sponsored partner in the task of removing workers from the labor force through retirement, albeit a partner that came at a cost. This view is wholly consistent with the metaphorical portrayal of Social Security as "contributory insurance," more like the private pensions that some employers were already providing, rather than the state/federal old-age poverty programs enacted in the New Deal that required some demonstration of need.

Conceptual support for integration is based on this view of Social Security, and goes beyond the value of integration as a cost-reduction measure enabling employers to sponsor pension plans they might not otherwise be willing to provide. If Social Security

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72. See discussion infra Part IV.
73. See discussion infra Part III.
74. See discussion infra Parts IV-V.
75. The old-age assistance program was contained in Title I of the 1935 Act and was financed through federal grants to the states, which administered the needs-based assistance payments to the elderly. See Social Security Act of 1935, Pub. L. No. 74-271, 49 Stat. 620 (codified as amended at 42 U.S.C. §§ 301-397(f) (1994)).
76. See generally SCHULZ & LEAVITT, supra note 14, at 3 (extending the defini-
is viewed as a pension plan with benefits based on a return on contributions and designed to provide adequate retirement income for low-wage workers, the notion of offsetting benefits available under a private pension against benefits payable under Social Security seems logical and appropriate.

Supporters of Social Security in its early days actively promoted the public belief that each worker was in effect “saving” for retirement through Federal Insurance Contribution Act (FICA) tax payments and that each worker’s benefits in retirement were essentially a payout of the worker’s contributions to the Social Security trust funds. This view has helped ensure broad political and popular support for the program for most of its history. Nonetheless, the private pension/contributory plan metaphor, however useful in explaining an intangible relationship between citizen, employer, and government, has been mistaken for the reality of Social Security as a social entitlement. The contributory financing structure of Social Security has been erroneously assumed to be the basis for entitlement when in fact the entitlement is earnings-based. This confusion is at least partly responsible for the persistence of integration in the face of repeated attempts at repeal.

E. Retirement Entitlements and Redistribution

Social Security has been portrayed as a public contributory insurance program, an earned right specifically vesting in each individual paying into the system. This view, consistent with American classical jurisprudential norms requiring the vesting of rights in
autonomous individuals, was used from the beginning of Social Security to build support for the program. It stresses the individual worker's responsibility for paying into the system and building a specific individual benefit entitlement through employment covered by Social Security. Redistribution of income from high-wage to low-wage workers is usually seen as inconsistent with this firmly established but narrow notion of individually earned entitlement.

Clearly, there is a difference between a social entitlement like Social Security—a claim on public resources based on publicly recognized criteria and political commitment to pay—and a vested individual property right, something like a bank account, or even more concretely, a store of cash in a trunk under the bed. Nonetheless, that distinction has never been clearly drawn in the public mind in discussions about Social Security. Certainly the redistributive element of the benefit formula, which results in low-wage workers getting higher proportionate benefits than high-wage workers, is neither widely understood nor publicly promoted as a goal of the program. Notwithstanding, redistribution was an integral element of the program from the beginning, and is essential to insuring adequate retirement income for low-wage workers.

Social Security's structure is a more or less deliberate attempt to separate social insurance, which is aimed at prospective needs in retirement, from needs-based welfare aimed at current needs that can be measured at the same time benefits are paid. The income redistribution provided in the Social Security benefit formula seeks to slow the decline into poverty of elderly persons who can no longer work and improve their own financial condition. Redis-

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81. See Simon, supra note 54, at 1452.

82. A graphic demonstration of the widespread popular belief that workers paying into Social Security are entitled to a specific account balance is the issue of the Social Security "notch," which was the subject of a congressionally appointed special commission in 1992. See THE COMMISSION ON THE SOCIAL SECURITY "NOTCH" ISSUE, FINAL REPORT ON THE SOCIAL SECURITY "NOTCH" ISSUE 1 (1994).

83. See discussion infra Part III.

84. See Wilbur J. Cohen, The Social Security Act of 1935: Reflections Fifty Years Later, in 50TH ANNIVERSARY EDITION REPORT OF THE COMMITTEE ON ECONOMIC SECURITY OF 1935 AND OTHER BASIC DOCUMENTS RELATING TO THE DEVELOPMENT OF THE SOCIAL SECURITY ACT 7-8 [hereinafter Cohen, CES 50TH]; see also discussion infra Part IV (describing the development of the modern retirement system).
tribution in this context is an essential part of the entitlement promise for those who have worked even though it may result in little or no change in the distribution of wealth generally. 85

If the essence of entitlement is predictability, Social Security benefits are the quintessential entitlement—benefits that bear a direct relationship to the worker's wage history will be paid, regardless of need when received or even when earned. In this context redistribution has only an indirect relationship to providing an adequate pension for low-income persons in retirement: Social Security redistribution is prophylactic, not corrective.

Many pension analysts continue to support at least limited forms of integration because they view Social Security as essentially similar to private pensions. 86 Their focus is on the goals of both systems, which are similar: providing income in retirement. But if the focus shifts to the context—the relationship between beneficiaries and paying workers—the distinction between Social Security and private pensions is clearer.

Private pension benefits are grounded in the relationship and promises made between employer and employee. In contrast, Social Security benefits are grounded in the relationship between the working and the nonworking public and on promises of social support based on a past history of productive employment. Decisions as to distribution of resources to the nonworking are made by society as a whole, through the Social Security benefit formula, not by the market or the employer as is the case in private pensions and investments.

Social Security benefits are based on a worker's employment history but are not part of the employer-sponsored system. The system is financed by employer and employee taxes but pays benefits based on service represented by covered earnings, not on contributions. Pension integration, therefore, essentially provides a refund to employers of a portion of the cost of income redistribution that Social Security otherwise requires them to finance for

all beneficiaries through payroll taxes. Integration is based on a mistaken conception of the Social Security entitlement, and is fundamentally inconsistent with the redistributive function of Social Security.

III. THE ROOTS OF ENTITLEMENT: EVOLUTION OF ENTITLEMENT AND RETIREMENT IN AMERICA

Retirement—the extended period of leisure after the end of a working life expected by most workers in the late twentieth century—is a recent phenomenon. While every human culture has some experience of supporting older members who live past the age of productive labor, it was not until widespread industrialization and the development of industrial-laboring and middle classes in Europe and the United States in the twentieth century that retirement became a relatively common occurrence.

Industrial capitalism transformed productive and commercial relationships in Western Europe from the fifteenth century onward, effectively eliminating the threat of generalized famine in most of Europe by at least the middle of the nineteenth century. At the same time, advances in medical science and hygiene began to diminish the threat of infectious plagues, which generally carried off the most vulnerable—children and the elderly. Thus, as industrialization began to generate surplus wealth, life spans began to lengthen, and the percentage of the population over age sixty began to increase. The need for and expectation of pensions and annuities for the aged is at least in part a product of industrial capi-

87. See Graebner, supra note 12, at 10-17.
88. See id.; see also Leslie Hannah, Inventing Retirement: The Development of Occupational Pensions in Britain 3-14 (1986) (comparing the development of British compensation schemes to those evolving in the United States).
90. See generally William H. McNeill, Plagues and Peoples 235-91 (1976) (stating that epidemics such as smallpox, tuberculosis, and syphilis were combated by a more systematic approach to medicine).
91. See David Hackett Fischer, Growing Old in America app. (1978) [hereinafter Fischer, Growing Old] (containing life expectancy tables and general discussion).
talism's prosperity and apparent triumph over catastrophic disease epidemics.92

Social Security was hailed at its enactment as a long overdue federal undertaking to guarantee direct income support for the nation's elderly, enabling them to retire without recourse to the poor house.93 Yet the federal government had previously assumed responsibility for providing income support in old age for a large proportion of the northern population in the form of the Civil War veterans' pensions.94 This pension system was based on earned entitlement—through military service—and presumed, rather than demonstrated, need.95 Before that, the Revolutionary War pension system96 had provided a precedent for federal pensions as an anti-poverty measure, breaking from the old system of locally controlled poor relief.97

Both of these systems, as well as the Social Security program that would be enacted in 1935, exemplified an American approach to dealing with poverty and old age in which the right to income was created by personal effort, not awarded based on need or status.98 Long before the enactment of Social Security, the Civil War pension system developed into the major federal entitlement program for the elderly just as the more direct sources of income for aged persons in pre-industrial America—principally control over income-producing land—were replaced by the uncertainties of industrial employment and economic cycles.99 The roots of our current earnings-based retirement entitlement system can be found in the history of these nineteenth century precursors. Their development helps to explain the cultural and political strength of retirement income entitlements.

A. Old Age and Poverty Before the Retirement Era

The most recent work on the history of retirement and the

92. But see LAURIE GARRETT, THE COMING PLAGUE: NEWLY EMERGING DISEASES IN A WORLD OUT OF BALANCE 30-52, 192-221 (1994) (analyzing the persistence of human vulnerability to microbial and viral diseases thought to be eradicated in the Western industrial world by the mid-twentieth century); MCNEILL, supra note 90, at 235-91.
93. See Report, CES 50TH, supra note 79, at 21-23.
94. See discussion infra Part III.B.
95. See discussion infra Part III.B.
96. See discussion infra Part III.B.
97. See discussion infra Part III.B.
98. See discussion infra Parts III.B-C, IV.
99. See discussion infra Part III.C.
elderly in America, and elsewhere, has yielded a complex portrait of the development of the concept of retirement as the natural end of a working life.\textsuperscript{100} It is clear that the current generation of retirees is the first to spend its entire adulthood more or less expecting to retire at a certain age.\textsuperscript{101} However, the work and family patterns of the American colonial experience provided a basis for all later old-age retirement income programs—entitlement for the worthy, charity, and grudging government assistance for the unworthy.

1. Old age and poverty in the old world

The notion of retirement necessarily rests on the ability of an economy to produce enough surplus wealth to support older non-workers.\textsuperscript{102} In agrarian societies generally up until the mid-to-late nineteenth century, advancing age was not automatically associated with cessation of work, which occurred only if and when actual physical incapacity set in.\textsuperscript{103} The pattern of frequent famine


\textsuperscript{101} See GRAEBNER, supra note 12, at 215-41.

\textsuperscript{102} The age at which children begin to be expected to be productive workers varies widely in both industrialized and nonindustrialized societies. It probably has as much to do with a society's overall level and equality of distribution of wealth as with its sophistication in Western terms. See generally PHILIPPE ARIES, CENTURIES OF CHILDHOOD: A SOCIAL HISTORY OF FAMILY LIFE (Robert Baldick trans., Vintage Books 1962) (1960) (presenting an in-depth discussion on the idea of childhood).

\textsuperscript{103} For the American experience, see FISCHER, GROWING OLD, supra note 91, at 40-49. See generally PHILIP J. GREVEN, JR., FOUR GENERATIONS: POPULATION,
and plagues that characterized Europe from the thirteenth through eighteenth centuries probably ensured that few of the poor survived to great ages; life past age sixty was largely reserved for the well-off bourgeoisie and the nobility who guaranteed comfort in old age through continued control of their wealth and families.\textsuperscript{104} In the absence of such accumulated wealth, the incapacity brought on by advancing age necessitated dependency on family, church, or local organized poor relief.\textsuperscript{105}

Before the late-nineteenth century, poverty in Europe was treated as a threat to the local social order, not as a curable condition. The English Poor Laws,\textsuperscript{106} enacted in the Elizabethan era, were designed to ensure public safety and order as much as to promote social welfare: "laws against the poor."\textsuperscript{107} These laws were in full effect in the seventeenth and eighteenth centuries, at the time of the first English settlements in the New World.\textsuperscript{108} They

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104. See Braudel, Everyday Life, supra note 89, at 90-91.
105. See Fischer, Albion's Seed, supra note 100, at 175-77; Katz, supra note 23, at 15. For a picture of the English approach to a growing poverty problem with which many American colonists would be familiar see David Underdown, Fire from Heaven: Life in an English Town in the Seventeenth Century (1992). During the sixteenth century the population of England grew by over fifty percent ... and for the towns most of the increase was concentrated in the last quarter of the century. ... The demographic explosion and the problems that stemmed from it—inflation, land shortage, unemployment, declining living standards for the ever-increasing numbers of the poor—determined much of the character of the century. The splendours of the age of Gloriana ... concealed even more misery and privation than was the common fate of ordinary English men and women throughout the country's history.

Population growth brought problems for Dorchester .... One such problem was poverty and the associated threat of disorder that came with it. A crescendo of anxious voices lamented the proliferation of the poor and unproductive .... Moralists constantly complained about the swarms of idle and dissipated young people who were not being contained within the system of household discipline—the system on which, most people believed, social stability depended .... As so often is the case, poverty was blamed on its victims. They hung about in alehouses, it was said, when they ought to have been working or worshipping .... Id. at 10-12.

106. For a full exploration of the development of the English Poor Laws from their origins in the Catholic Church's canon law requiring aid to the poor, see Larry Cata Backer, Medieval Poor Law in Twentieth Century America: Looking Back Towards a General Theory of Modern American Poor Relief, 44 Case W. Res. L. Rev. 871, 938-65 (1995).
108. See Backer, supra note 106, at 964.
\end{footnotesize}
were designed to provide local care for the poor of the locality and to drive away migrant poor with no local connections. In fact, the treatment of the poor throughout Europe during this period was largely designed to eliminate the risk to political stability represented by large groups of starving peasants invading urban areas while still providing care for the poor of the town or locality.

Age appears not to have been seen as reason in and of itself for failure to work—all were generally expected to work as long as they were physically able to—but those elderly who were no longer able to provide for themselves were generally part of the "deemed worthy" group, along with the disabled, and thus entitled to charitable relief. The poor-relief system, from medieval canon law to the sixteenth century English laws, assumed that the elderly who could no longer work would be largely cared for by their families. In the absence of families or independent assets, only "town-born" poor elderly could expect to be cared for adequately by the local public.

109. See id. at 953-57.

The major characteristics of the Elizabethan system of poor relief included primary family responsibility for the maintenance of its members, public responsibility for the relief of the poor at the local level, encouragement of private charity, and relief tied to residency.

Every English subject had a settlement roughly corresponding to a person's place of residence. Only those who had a settlement in a community were entitled to its aid. Paupers who remained in a community in which they were not settled were to be excluded or expelled from the community and returned to the community of settlement.

Id. at 953-56.

110. See id. at 952.

At least in England, the state imposed a secular obligation to work, on pain of imprisonment. As such, reinforcement of the social order through the poor relief system found expression in the tendency of medieval poor law systems to criminalize vagrancy as a violation of compulsory work laws, to reduce the incentives of an unemployed adult populace to engage in antisocial activities. Thus, the ecclesiastical poor law system tended to rely on secular criminal law to penalize the able-bodied, who were supposed to be working for their bread instead of begging for it, for the sin of nonproductivity.

It is in the context of this fully developed ecclesiastical system that the English poor law system arose.

Id.; see also Braudel, Everyday Life, supra note 89, at 74-76 (stating that European attitudes toward the poor hardened in response to the increasing threats of famine and plague); Robert Hughes, The Fatal Shore 19-27 (1987) (describing rising poverty levels and lack of remedies in eighteenth century England and the resulting crime waves that accompanied increasing population and poverty).

111. See Backer, supra note 106, at 943 n.213.

112. See id. at 943.
2. Colonial American approaches to poverty and aging

In pre-industrial America—the colonial period up until about the Civil War—the family-based, largely agrarian economy required and allowed work until disability from extreme old age or death.\(^\text{113}\) For those without control of property or income, extreme old age in the pre-Civil War era was inextricably linked with dependency, either on family or on local charity.\(^\text{114}\) American colonists took the same geographic approach to poor relief as their English forebears had: the poor of the town, those known to the locality, were generally cared for if they were "of good character" and unable to provide for themselves, but the vagrant poor were a threat to social stability and were shunned, if not actively driven away.\(^\text{115}\)

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113. See HABER & GRATTON, SEARCH FOR SECURITY, supra note 100, at 89-90.
114. See id. at 90. Not all elderly people in the colonial period, though, had access to prestigious work or a comfortable retirement. These old persons found the last years to be quite different. Landless aged men spent their final days intermittently employed as laborers. Others discovered that their declining strength made work impossible. Wandering from town to town or begging alms from neighbors, they received, at best, charity, and at worst, scorn and neglect.

Id. (footnote omitted). The scope of this Article does not permit an extensive discussion of the debate among historians as to when the elderly became objects of pity and scorn rather than respect.

115. According to Fischer, social stratification in eastern England where most Puritan immigrants came from was "marked by inequality in high degree." FISCHER, ALBION'S SEED, supra note 100, at 175. Land was overwhelmingly held by great landowners or the Church of England.

At the bottom of this social order were large numbers of desperately poor people: small leaseholders and landless laborers. Most adult males held fewer than five acres. A majority possessed no land at all. In the late sixteenth and early seventeenth century, the poor were increasing more rapidly than the population as a whole.

Id.

Small landowners and landless workers were not at the lowest rung of the English social ladder. "At the bottom was a large vagrant population of wandering poor who overran the larger towns and much of the countryside as well." Id. at 176. Towns hired "Beadles" to gather up the beggars and drive them out of town limits. See id. "Chronic unemployment was a major problem throughout the region. In the year 1630, many poor men and women, 'complaining for want of work' were given make-work jobs by the towns." Id. Treatment of the elderly poor depended on where they came from.

Most towns looked after their own; their records show that elderly residents were often treated with decency, respect and compassion. . . .

But the vagrant poor were treated with great brutality. Pregnant women were expelled so that their newborn babies would not become a charge upon the town. . . . Some of these vagrants were sent to the county gaol . . .

. . . Others went to houses of correction and almshouses. The lucky ones
In the context of frontier agrarian and small town center economic structure, the presumption appeared to be, as it had been in England, that persons without means and outside their own homeplace beyond the reach of their kin were suspect and not worthy of charity. Clearly it would be easier to determine whether an individual was worthy of assistance if the local authorities were familiar with that person's background and current circumstances. In effect, the geographic approach was one way of enforcing a moral test of "worthiness." Aid took the form of "outdoor relief"—aid given to those still living outside of almshouses and financed by town revenues and the proceeds of liens on, or liquidation of, the pauper's property. Local officials also solved the local poverty problem by placing indigent individuals with other families, or occasionally, selling the impoverished person, or less drastically the indigent's belongings, at public auction.

The poor elderly were not especially differentiated from the disabled. They were more likely to be considered worthy of assistance if they were unable to work and without resources or family to look to for food and shelter, so long as they were recognized as "local." In effect, colonial Americans, like their European contemporaries, used local identification as a way of separating the "deserving" from the "undeserving" poor.

This "modernization" of colonial society... was accompanied by the evolution of poverty from an occasional to a systemic problem. Poverty, in turn, was but one part of a transformation that involved occupational specialization, redistribution of wealth, spreading commercialization, decay of familial institutions, social atomization, and the legitimation of personal interest...
3. Retirement for the propertied

While retirement, in the sense of voluntary cessation of work in old age, was not unknown before the late-nineteenth century, it was relatively uncommon and was a prerogative of the propertied. Well into the beginning of the twentieth century, most American men remained in the paid labor force after age sixty-five, presumably as long as they were physically able to work and needed the income. Indeed, for the minority who survived into old age, care and comfort beyond the point at which they could no longer work was largely ensured by control over family property, and with it, over sons and daughters. Thus, the identification of age with poverty that became part of the "social question" for reformers early in the twentieth century had not yet been made in pre-Civil War America.

Nonetheless, some elderly men and couples in the pre-Civil War era retired from their farms, usually to small towns or villages. For many small farmers and artisans, retirement may not

121. See HABER & GRATTON, SEARCH FOR SECURITY, supra note 100, at 88-93.
123. See HABER & GRATTON, SEARCH FOR SECURITY, supra note 100, at 89-91, 104-06. The importance of ownership of property to a worker's ability to stop work is demonstrated by wide regional and racial differences in rates of retirement. For example, during the slave period, African Americans held in chattel slavery in the South were expected to, and largely did, work until death. See id. at 92-93. However, even after emancipation, the establishment of a sharecropping/plantation regime that in many ways replicated the conditions of servitude meant that retirement was not an option for most older African Americans until after World War II. See id. at 94-95.
124. See HABER & GRATTON, SEARCH FOR SECURITY, supra note 100, at 93-94. Many appeared to have left the farm, moving to villages and small towns . . . Such households were unique for the low and steadily falling labor force activity of older men; between 1860 and 1910, the percentage of older men
have meant a radical change but rather simply a gradual decrease in work activity depending on the adequacy of savings or other arrangements for support in old age. A frequent pattern for the nineteenth century farmer reaching old age was to lease or give parts of the family farm to the next generation in exchange for staying on the farm and continuing to work it, producing family income for both generations. Those farmers who controlled property and assets could stop working in old age and still be assured of income from the next generation whose continued support was guaranteed by the older generation's control of the farm or business.

The elderly poor without family were treated similarly to other poor individuals who were unable to work even though extreme old age probably carried with it a presumption of inability to

in villages and small towns who reported occupations fell from 74 to 44, a much steeper decline than in farm or urban households.

Id. (footnote omitted).

125. See, e.g., Kathleen Neils Conzen, Peasant Pioneers: Generational Succession Among German Farmers in Frontier Minnesota, in CAPITALIST TRANSFORMATION, supra note 100, at 259, 267-76 (describing the ways in which the parent farmer and spouse would bargain with an adult child to take over the bulk of the farming as the older generation gradually reduced their work activity).

126. See id.; see also HABER & GRATTON, SEARCH FOR SECURITY, supra note 100, at 89-90 (discussing how the "aging landholder managed the business of the farm, controlling the careers, marriages, and wealth of... heirs"). According to the latter, elderly widows of means also can be found in census data from this period as having "retired" from their children's households to set up independent homes, again usually in small villages or towns. See id. at 91. Nonetheless, single women and widows faced considerable economic uncertainty if they survived to old age and were largely dependent on provisions for control of income made by deceased husbands or fathers in order to avoid dependence on family or local charity. See id. at 90-91.

Other husbands provided for wives through maintenance contracts, a form of annual pension... These wills detailed both the widow's rightful assets and the obligations her heirs owed her so long as she remained unmarried. For the most part, they compelled women to retire from active management of the farm, giving over authority to the next generation.

Id. at 90. As for poor women, "[p]ublic relief records, the charity dispensed by ministers, and the early private organizations directed toward needy aged women showed that many ended their lives as members of the 'deserving poor.'" Id. at 91.

127. See HABER & GRATTON, SEARCH FOR SECURITY, supra note 100, at 89-90.

Older property owners remained closely involved in farming and with the family that provided a labor supply; they continued to be active participants in the preindustrial enterprises that combined land and labor... Based in the family farm economy, such authority provided the majority of older men and women with a setting for vigorous economic activity and high social standing. Since the farm was the central productive unit and age led to ownership, older men and their wives possessed impressive resources and often worked or managed a work force until late in life.

Id. (footnote omitted).
work. Still, there were comparatively few such elderly poor to start with before the late-nineteenth century, and certainly those few had a claim on parish or local relief institutions such as the almshouse.  

In summary, throughout the pre-industrial period aged Americans apparently placed a high value on independence and control over their living arrangements; where multigenerational households existed, more often than not the older generation kept control of property and therefore income. The sentimental popular picture of respected elders living with their children in harmony was not complete mythology, but it certainly was not the rule. Even in the Puritan culture, which David Hackett Fischer and others describe as especially deferential to elders, deference was apparently based in substantial part on the older generation holding onto family land long into the adulthood of the next generation. Entitlement to comfort in old age, in this era, was based quite literally on holding the deed to the family farm.

**B. The Federal Pension Model: Veterans' Entitlements**

The Social Security system that emerged in the late 1930s echoed in important aspects the principles and categories of coverage provided under the Civil War pension program. A comparison of the Revolutionary War and Civil War pension systems with the benefits provided under the Social Security Act after 1939 reveals strong similarities between the programs in goals, assumptions, and themes, which have persisted for 175 years of federal income support programs.

First, it appears that aid to the elderly, veterans or not, had a strong poverty-prevention element whether or not poverty was a

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128. See generally id. at 20-47 (discussing the role of families in the lives of the elderly).

129. See id. at 22-27. Roughly the same pattern could be seen in England during the same period. See HANNAH, supra note 88, at 3-5.

130. See HABER & GRATTON, SEARCH FOR SECURITY, supra note 100, at 29-40.

131. See FISCHER, ALBION'S SEED, supra note 100, at 109-10.

Respect for age rested upon a solid material base. The system of landholding in New England was purposely used to maintain a proper attitude of subordination in the young. Puritan elders tended to retain land for an unusually prolonged period. Sons who married at twenty-five or twenty-six sometimes did not receive land of their own until well into their thirties, and continued in a state of dependency upon their aged parents.

Id. (footnote omitted).

132. See generally SKOCPOL, PROTECTING SOLDIERS, supra note 100, at 102-30 (discussing the development of the Civil War pension program and its legacy).
requirement for receipt of aid; presumptive, rather than demonstrated, need was the trigger for benefit payment. Second, we can conclude from the structure of these programs that only those who matched a consensus view of worthiness—war service, inability to work because of age or disability, or both—were viewed as entitled to public support. Citizenship or residency alone was an insufficient basis for the right to adult income support. 133

Finally, although there is substantial evidence of late-nineteenth and early-twentieth century patterns of individual saving for the possibility of retirement in old age, individual efforts alone were not likely to provide sufficient economic security in old age to induce retirement. Those older men who did leave the work force up until the 1920s were most likely to have based their retirement security on publicly provided pensions. 134

1. Revolutionary War pensions: welfare for the deserving

The first American federal antipoverty program was the Revolutionary War Pension Act, enacted in 1818 and expanded in 1820. 135 The program provided annual lifetime benefits for Revolutionary War veterans who could demonstrate lack of income or assets at the time of initial application for benefits. 136 While enactment of the program was probably a response to nationalism aroused by the War of 1812 and sympathy for the plight of Revolutionary War veterans in dire economic circumstances, the pensions paid under the 1820 Act had many of the characteristics of old-age pensions designed to prevent poverty in old age resulting from inability to work. 137

Unlike the later Civil War system, the Revolutionary War pension program required an initial demonstration that the vet-

133. See id.; see also HABER & GRATTON, SEARCH FOR SECURITY, supra note 100, at 71-87 (describing aid to the elderly during the industrial and Social Security eras).
134. See HABER & GRATTON, SEARCH FOR SECURITY, supra note 100, at 104-06.
136. See id. (“Recipients and an estimated 60,000 members of their households received aid for an average of nine years at a total cost of $22,000,000.”).
137. See id. at 171-72.

Congress rejected the traditional argument that republican principles were incompatible with the creation of a military pension establishment or with federal charity to a “rank of society.” The new attitude stressed that the Republic's heritage would be dishonored and its principles tarnished unless the nation aided its “heroes of the Revolution” who were suffering in poverty.

Id. (footnotes omitted).
eran was in need to establish eligibility for benefits. In a sense, this program was based on a double test of worthiness, as service to the Republic in war as well as demonstrated poverty were required for receipt of benefits.\textsuperscript{138} However, once sufficient poverty was initially established, veterans received pension benefits for the rest of their lives without further inquiry into their economic status.\textsuperscript{139}

We can see in the Revolutionary War pension program the beginning of the prophylactic approach to poverty for those deemed socially worthy that is epitomized today by the Social Security program. The first veterans of an American war were deemed worthy by virtue of their war service, and thus, once they demonstrated need, were given a fixed pension amount, enough for a "comfortable and frugal existence," without being required to demonstrate specific needs again later in life.\textsuperscript{140} As a result, these pension recipients were independent of local authority supervision or control and were not subject to the degradation of being placed with families or of having their belongings sold at public auction. Because their entitlement was based as much on their service as veterans as on their poverty, receipt of the pension meant independence and insulation from the control over daily life that awaited recipients of town poor relief.

2. The Civil War pension system: precursor to social insurance

The Civil War was the first American "modern" war with participation by a large proportion of the military-age adult male

\textsuperscript{138} See id at 172. ("Pensions were awarded to veterans . . . who swore that 'they were in need of assistance from their country'.")

\textsuperscript{139} Under the 1820 program, the Attorney General and the War Department allowed only the poorest veterans to qualify and established a "poverty line" as a test of sufficient poverty. See id.

In 1820, because of a flood of applicants, Congress tightened the poor-law provisions of the act by adding a means test. Veterans wishing to continue on the pension rolls as well as new applicants had to report their residence, occupation, health, income, debts, and an inventory of real and personal property to the War Department. Also, they were to provide the age, gender, physical condition, and relationship of all others in their household and any sources of aid rendered the applicant. Furthermore, the War Department required a codicil containing a court's assessment of the value of the veteran's property. Finally, the War Department established an unofficial poverty line to help separate deserving from undeserving applicants. The attorney general ruled that only applicants "in the lowest grade of poverty" deserved the benefit. Over 18,000 of the 20,000 applicants passed the means test.

\textsuperscript{140} Id. (footnote omitted). At least half of these pensioners were over age 65, and about 3% were over age 80. See id. at 173.

\textsuperscript{140} Id. at 173 (footnote omitted).
population rather than primarily professional soldiers, a phenomenon that led directly to the formation of the United States' first mass-scale federal social welfare program, the Civil War pension system.\textsuperscript{141} By 1910 the Civil War pension system was paying benefits in some areas for up to 20% of all persons age sixty-five and over, a rate comparable to the coverage provided by German and Danish old-age social insurance programs at that time.\textsuperscript{142} Since as late as 1900 two-thirds of men over age sixty-five were still gainfully employed,\textsuperscript{143} it is likely that Civil War pensions provided a source of income for a large portion of elderly men who were no longer working or at least not working at the level of self-support.\textsuperscript{144}

The Civil War democratized military participation. The entire adult male population was subject to conscription, in both the North and the Confederacy, even though most soldiers volunteered for duty until late in the conflict.\textsuperscript{145} It was a conflict of unprecedented scale and ferocity. Over the four years spanning 1861 to 1865, over 2.2 million men—about 37% of northern men between the ages of fifteen and forty-four in 1860—served in the Union forces.\textsuperscript{146} Of those, almost 365,000 died from combat, illness, or war-related misadventure.\textsuperscript{147} By way of comparison, only about one-third of British men—also largely nonprofessional sol-

\textsuperscript{141} For a general discussion of the Civil War pension system, see SKOCPOL, PROTECTING SOLDIERS, \textit{supra} note 100, at 102-30. \textit{See also} Megan McClintock, Binding up the Nation's Wounds: Nationalism, Civil War Pensions and American Families, 1861-1890 (1994) (unpublished Ph.D. dissertation, Rutgers University) (on file with the Loyola of Los Angeles Law Review) (analyzing the Civil War pension system as a family support program expressing a new sense of nationalism and patriotism). Similar although less extensive pension programs were set up by the various Confederate states for Confederate veterans and their families. \textit{See} SKOCPOL, PROTECTING SOLDIERS, \textit{supra} note 100, at 139-43.

\textsuperscript{142} \textit{See} SKOCPOL, PROTECTING SOLDIERS, \textit{supra} note 100, at 132.

\textsuperscript{143} \textit{See} ACHENBAUM, \textit{supra} note 122, at 105.

\textsuperscript{144} \textit{See}, e.g., SKOCPOL, PROTECTING SOLDIERS, \textit{supra} note 100, at 129 ("Over time, Civil War pensions became more and more obviously old-age and survivors' benefits for the veterans.").

\textsuperscript{145} \textit{See} McClintock, \textit{supra} note 141, at 52-64, 124; \textit{see also} 1 SHELBY FOOTE, \textbf{THE CIVIL WAR: A NARRATIVE} 394, 406 (1958) (discussing the Confederacy's proposal to institute conscription).

\textsuperscript{146} \textit{See} BUREAU OF THE CENSUS, U.S. DEPT OF COMMERCE, \textbf{HISTORICAL STATISTICS OF THE UNITED STATES, COLONIAL TIMES TO 1970} at 1140 (1975); SKOCPOL, PROTECTING SOLDIERS, \textit{supra} note 100, at 103 (Skocpol calculated the 37% figure using these census numbers.).

\textsuperscript{147} \textit{See} SKOCPOL, PROTECTING SOLDIERS, \textit{supra} note 100, at 103.
diers—served in World War I. As for casualties, by the end of the Civil War, eighteen out of every one thousand northern citizens had been killed in connection with the conflict. By comparison, 3.14 soldiers per thousand Americans died in World War II. Equally important is the number of men who returned home wounded—a total of almost 300,000 soldiers—constituting about fourteen of every one thousand Northerners.

From the beginning, the Civil War pension system provided benefits for those injured or harmed as a result of military service during the war and to the widows, orphans, and certain other dependents of soldiers who died “for causes traceable to their Union military service.” While benefits initially were distributed based on the severity of the disability and on military rank, eligibility was not based on demonstrated need, and pensions, once granted, were paid for life. Federal protection against a decline into poverty for families of Civil War soldiers was not extended out of detached altruism. Once it became clear that the war was going to be both lengthy and extremely bloody, it became more difficult to fill the ranks with volunteer soldiers without some assurance that families left behind would be cared for.

Nonetheless, the fact that family benefits were initially included as part of the Civil War pension scheme is evidence of their underlying purpose: to compensate soldiers and their families for losses suffered during the war, inevitably including lost or diminished capacity to earn and support those families. The para-

148. See id.
149. See id.
150. See id. at 103-04.
151. See id. at 104.
152. Id. at 107.
153. See id. at 107-12.
154. See McClintock, supra note 141, at 78-98.
   While bounties and pay advances provided some relief to families of volun-
   teers, Northerners continued to blame family obligations for the slow pace of enlistment in the summer of 1862. ... [L]ocal relief and federal recruit-
   ment measures failed to reach relatives of soldiers who never returned home. All forms of public aid went only to families whose breadwinners were in the military; payment stopped with a soldier's discharge or death. Thus the specter of destitute widows and orphans continued to deter many able-bodied men from enlisting.

Id. at 82 (footnotes omitted).
155. See SKOCPOL, PROTECTING SOLDIERS, supra note 100, at 107 (“Under the 1862 law, widows, orphans, and other dependents of those who died for causes trace-
   able to their Union military service also received at the rates their relatives would have gotten for total disabilities.”); see also McClintock, supra note 141, at 96-109.
mount goals of the original legislation were prevention of destitution, avoidance of local almshouses, and aid to the poor for this class of Americans viewed as worthy of assistance but "too good" for ordinary poor relief.\textsuperscript{156} This goal was reiterated in the legislation's repeated expansions from 1862 through the end of the century.\textsuperscript{157}

The Federal Civil War pension system was initially a response to the inadequacy of local poor relief and volunteer charity to provide for dependents of current and deceased Civil War soldiers during the war.\textsuperscript{158} Both the scale and length of the war meant that local and voluntary efforts would prove insufficient. Even though states overrode the limits of strictly local poor relief and passed tariffs, excise taxes, and other measures to finance aid to military families, ultimately federal aid was required.\textsuperscript{159} The most significant aspect of this system, from the perspective of the later development of retirement entitlements, was the absence of any requirement for demonstration of need.\textsuperscript{160} Payment of benefits was based on a presumption of need arising from the inability to work because of injuries received in the war or, in the case of family benefits, absence of the male breadwinner.\textsuperscript{161}

After the war ended a series of congressional expansions of the program—both in the amount of pensions and in the categories of soldiers and dependents eligible for benefits—effectively transformed a military disability pension system into a broad-scale old-age and disability family benefit system.\textsuperscript{162}

\textsuperscript{156} See SKOCPOL, PROTECTING SOLDIERS, \textit{supra} note 100, at 148-51.

\textsuperscript{157} See id. at 106-10; see also McClintock, \textit{supra} note 141, at 96-109 (commenting that the government's largesse was not confined to widows and orphans but extended to mothers and sisters of soldiers).

\textsuperscript{158} See McClintock, \textit{supra} note 141, at 96-109.

\textsuperscript{159} See id. at 80-81.

Military families received assistance from a variety of sources in mid-1862. Despite attempts to place volunteers' families in the hands of private benevolence, the need exceeded the resources of charitable associations. Municipalities continued to levy funds for the relief of dependents during the first half of 1862, but the strain of meeting the growing need began to show after Shiloh. . . . States broke with the tradition of local relief and expanded their welfare activities to meet the rising demand for aid to families.

\textit{Id.}

\textsuperscript{160} See SKOCPOL, PROTECTING SOLDIERS, \textit{supra} note 100, at 106-07, 148-50.

\textsuperscript{161} See id.

\textsuperscript{162} See id.
Between 1880 and 1910, the U.S. federal government devoted over a quarter of its expenditures to pensions distributed among the populace; aside from interest payments on the national debt in the early 1880s, such expenditures exceeded or nearly equaled other major categories of federal spending. By 1910, about 28 percent of all American men aged 65 or more, more than half a million of them, received federal benefits averaging $189 a year.163

Liberalization of benefits, along with the dual impact of gradual aging and lingering minor wounds on the ability of aging veterans to support themselves, resulted in increasingly higher numbers of beneficiaries and expenditures under the program, peaking in the mid-1890s.164 Congress ultimately severed the direct connection between injury and benefit eligibility and repeatedly raised benefits throughout this period.165 Thus, as Civil War veterans aged and their earning capacity diminished regardless of any injuries they may have received in the war, the basis for the presumption of inability to earn was broadened from physical disability to simply old age, and benefits became a more significant part of total income.

Theda Skocpol estimates that by 1910, about 18% of all United States residents aged sixty-five and over were receiving benefits. This number included 28.5% of all elderly men, plus approximately 8% of all elderly women who were receiving survivors' benefits.166 These percentages were comparable to northern European old-age pension systems in effect at the time.167 Moreover, benefits were available at younger ages—at least at age sixty-two and frequently earlier—in more substantial amounts, and for more dependent family members, than under most European systems at the turn of the century.168 In 1910 German old-age benefits

163. *Id.* at 65 (footnote omitted).
164. *See id.* at 110 fig. 1.
165. *See id.* at 110-11. The 1890 Dependent Pension Act provided benefits for any veteran who had served for at least 90 days during the war if he became unable to do manual labor at any point. *See id.* at 111: “In practice, old age alone soon became a sufficient disability, and in 1906 the law was amended to state this explicitly. After the turn of the century, moreover, Congress several times significantly raised the general benefit levels for both veterans and surviving dependents.” *Id.* at 111.
166. *See id.* at 132.
167. *See id.* at 132-34.
168. *See id.* at 131-34.

German old-age and disability insurance failed to cover surviving depend-
averaged about 18% of the typical worker’s income, and British pensions averaged about 22%. In contrast, the average United States Civil War pension benefit in 1910 equaled about 30% of the average annual income of all employed Americans.  

Thus, during the period in which the United States became an industrial nation—as millions left the farms and joined the ranks of industrial workers, disrupting the property-based family and village network of support for the elderly—a federal support system developed to provide for at least a large minority, and perhaps a majority, of older workers who could not support themselves in old age. Given the high labor force participation rates of men over sixty-five well into the twentieth century—at least 60-70% by most estimates until after 1930—it seems likely that most older men who could not or did not wish to work past age sixty-five had a federal or state veterans' pension to fall back on. Widows and orphans of those who died during the war or of war-related causes were also supported by the federal system so that a substantial support network lasted into the twentieth century, even after the war generation was gone.

The Civil War pension system was contributory only in the sense that its beneficiaries sacrificed their health, youth, and the financial security of their families in service to the Union. But in most other respects, the hallmarks of eligibility under this system resemble those of the Social Security system enacted in 1935 and 1939. The characteristics that distinguished the American approach to social welfare from that of the rest of the industrialized world were fully developed in the Civil War pension system and

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Id. at 132-34 (footnotes omitted).

169. See id. at 134-35.

170. See generally Roger L. Ransom et al., Inventing Pensions: The Origins of the Company-Provided Pensions in the United States, 1900-1940, in Societal Impact, supra note 99, at 1, 5-6 (commenting on the importance and prevalence of healthy savings accounts of these older workers).


172. See id. at 134.

173. See id. at 148-50.

174. See id. at 103-04, 149-51.
represent a continuum from the Revolutionary War system. Benefits to those unable to provide for themselves would only be given to those who had "earned" them—either through public or military service or later through sufficient time in the industrial work force.

The common thread running from Revolutionary War veterans' benefits through Civil War veterans' benefits to Social Security retiree benefits is the need perceived by the public and the Congress for a pension entitlement based on presumed rather than demonstrated need. Entitlement was viewed as essential in order to preserve the independence of those who had, in one way or another, earned their benefits, to insulate them from intrusive poverty programs and their overseers—whether village elders or welfare office bureaucrats. This insurance against falling from one's place, both economically and socially, became more critical as industrialization broke up older patterns of aging and family care and as industry and government considered the popularization and democratization of old-age retirement.

C. Industrialization and the Beginning of "Voluntary" Retirement

Historians differ as to the exact effects of industrialization on older workers and on the extent to which employers purposely used age and seniority to exacerbate unemployment among the old. Nonetheless, there can be no doubt that by the early-twentieth century, the nature and organization of work for most Americans and Europeans had shifted from the agrarian family
economy to an urban industrial economy in which the family and the elderly had different roles than in the pre-industrial world. While most older workers were capable of continuing to work past age sixty-five, and did so at least up to the 1930s, they had to de-

178. All of the studies cited above address the issue of industrialization and the change in working patterns to one degree or another. For a detailed study of the change in rural economies early in the nineteenth century with the coming of industrialization, see Jonathan Prude, Town-Factory Conflicts in Antebellum Rural Massachusetts, in CAPITALIST TRANSFORMATION, supra note 100, 71-102.

179. Whether one views the labor force participation of older American men as a sign of continued employment in old age, or of the beginning of widespread retirement seems to be a matter of perspective. For example, Orloff appears to see retirement in reality as involuntary unemployment, resulting from the pressures of speedy and innovative production that increased after the turn of the century.

[In the United States, analyst Murray Latimer found that the decline in labor force participation for males aged sixty-five or over (as well as that for males aged between forty-five and sixty-four) between 1890 and 1920 was accounted for entirely by the decline in nonindustrial employment. There was almost no decline in the participation rates of older American men in industry or in agriculture over the period 1890-1930; total rates did drop off, for rates in the industrial sector were lower than in the agricultural, and the occupational distribution was shifting away from agriculture. In his study of the elderly in Boston, historian Brian Gratton reports that in urban areas like Boston, older men's labor force participation—almost entirely within nonagricultural sectors—was quite stable over the forty years between 1890 and 1930; indeed, in the fifty largest American cities, the rate fell only eight percentage points, from 61 percent to 53 percent. Gratton argues that a new equilibrium level of participation in the labor force may have been reached within industrial occupations, and that there was no inherent reason why healthy aged workers could not have gone on working. Gratton and others stress that it was after the introduction of old age assistance and insurance measures that overall participation rates dropped sharply in [the United States, Britain, and Canada].

... The aged were disproportionately represented in traditional jobs and underrepresented in newer occupations, so that as the composition of the labor force changed, there was less room for older workers. ... What was problematic for older workers was not the introduction and use of new industrial technology per se, but the speed with which the machinery had to be operated. ... As the concern with rationalization and efficiency grew, so too did the notion that the aged were by definition "superannuated" and unfit for participation in the labor force.

ORLOFF, supra note 100, at 100-01 (citations omitted).

In contrast, Carter and Sutch look at approximately the same data on labor force participation and conclude, based on their research into labor patterns of self-employed workers who apparently ceased work voluntarily, that many men planned their retirement by saving; investing in assets such as land, tools, shops, and inventory; becoming self-employed; and eventually ceasing productive activity and presumably living off the stream of earnings generated by their assets. In their economic independence from both paid labor and the support of grown children, these were "modern" retirees.

... We develop evidence to suggest that voluntary retirement was not uncommon in the past. Individuals saved in order to be able to retire. ... Many men voluntarily left the wage sector long before retirement age to
velop different strategies for survival in the industrial world when economic adversity struck, whether because of economic downturn or technological advances that made skills obsolete.

However, far from severing the ties between generations, the industrialization of work may have made the older generation more directly dependent on the younger generation, resulting in a new "family strategy" that relied on household income from wage earnings. What made this strategy different from that of earlier generations was that the older generation was less likely to hold the economic power—the deed to the farm for example—that earlier in the century provided some assurance that the younger generation would support aged parents until death. In addition, medical advances made it increasingly likely that the older generation would live well beyond the point of capacity for full-time, self-sustaining employment, particularly in the increasingly "rationalized," efficient, and time-conscious factory settings that began to dominate the workplace at the beginning of the twentieth century.

For social reformers in the 1920s such as Abraham Epstein, one of the early agitators for social welfare and old-age programs in the United States, it seemed that industrialization had brought unmitigated horrors upon the elderly who in an earlier time would have found shelter and care on the family farm:

Modern industry finds little use for [older] workers. It replaces and discards these aged wage-earners as it is in the habit of replacing and discarding the worn-out and inefficient machinery. . . . Modern machine industry [has] less need for expertness and experience and greater use for speed and rapid production. As a result, the younger generation, though less experienced, is continuously crowding out the older and less efficient workers.

work for themselves. Self-employment thus facilitated rather than postponed retirement.

Carter & Sutch, supra note 177, at 6-7. These differing views are not necessarily contradictory, although Carter and Sutch may be underestimating the importance of Civil War pensions in supporting both self-employment and retirement among the approximately one-third of men over age 65 who were not working in the 1890-1920 period.

180. See Gratton, supra note 171, at 51-63.
181. See id.
182. See HABER & GRATTON, SEARCH FOR SECURITY, supra note 100, at 95-110.
183. See id. at 27.
184. Id. at 96.
In fact, the picture was a good deal more complex than that. For one thing, industrialization and its twentieth century expansion of production methods and mass consumption of manufactured products contributed to the creation and dissemination of the great wealth that was necessary for any economy to be able to support substantial numbers of the nonworking.\(^{185}\)

Nonetheless, while industrialization did not create old-age poverty, the transition from farm to urban wage work, combined with lengthening life spans, undoubtedly made the threat of poverty in old age more real. This appears to have been particularly true as rapid technological advances made successive sets of skills obsolete. For older workers such changes required either acquisition of new skills, or if the means were available, retirement or a shift into self-employment of one sort or another.\(^{186}\) Industrialization brought with it an inherent insecurity of wage employment in an economy marked by periods of severe economic downturn that was substantially different from the experience of most earlier generations.

This increased insecurity of employment, which accompanied industrialization, may have led to increased identification of poverty with old age even though the majority of the elderly were neither in poverty nor in the poorhouse. Although most of those over sixty continued to work and maintain households alone or with their children, the possibility of poverty and the threat of the poorhouse were the fears, if not the reality, of the majority of older workers in the early part of the century.\(^ {187}\)

Even though there seems to have been, from the latter part of the nineteenth century up to the 1930s, a sizable retired population of one-quarter to one-third of men over age sixty-five, leaving work for leisure upon reaching age sixty-five or earlier was still not the mainstream expectation for most Americans until after World War II.\(^ {188}\) It seems most likely that the retirement decisions were influenced, as is frequently the case today, by the expectation of a steady income stream in the absence of work and by opportunities to work, improved health, and other factors. Given the payment

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185. See Orloff, supra note 100, at 277-78.
187. See Orloff, supra note 100, at 3-5, 91-92; see also Carole Haber, Over the Hill to the Poorhouse, in Societal Impact, supra note 100, at 90-129 [hereinafter Haber, Over the Hill] (discussing use of the threat of institutionalization in the movement to pass national welfare measures such as Social Security).
188. See Ransom et al., supra note 170, at 5-6.
of Civil War pensions to almost 30% of men over sixty-five through at least 1910, the retirement option for many of those listed as retired in the census data of 1900 and 1910 must have been supported by the federal benefit.

Industrialization alone did not automatically make older workers superfluous, particularly those with education or skills that could be adapted to changing technologies. Despite evidence of life-cycle savings patterns in the early years of the century, perhaps to finance retirement, the possibility of retirement still seems to have been reserved for the minority with incomes high enough to allow such savings or with access to a stream of income from property or from Civil War or other government pensions. Retirement was not yet the norm for workers who reached age sixty-five or even seventy.

IV. EXPANSION OF ENTITLEMENT: THE MODERN RETIREMENT SYSTEM

The U.S. retirement income system developed slowly from the mid-nineteenth century through the enactment and expansion of the Social Security system and later of the Employee Retirement Income Security Act (ERISA). Indeed, it is difficult to tell which came first—the practice of and desire for retirement or the pensions necessary to support retired workers. Clearly, the vague popular picture of industrialization pushing older workers out of the work force and into poverty, from which they would eventually

189. See Carter & Sutch, supra note 177, at 9. While I disagree with many of the conclusions drawn in their article, and with the authors’ oversimplification and mis-statement of a “traditional view” of the origins of retirement—one that does not appear to be held by most historians currently working in the field—this is nonetheless an interesting and useful analysis on the employment patterns of older male Americans in this period. See also Haber & Gratton, Search for Security, supra note 100, at 77-79 (discussing individual savings through “tontine” insurance policies); Roger L. Ransom & Richard Sutch, Tontine Insurance and the Armstrong Investigation: A Case of Stifled Innovation, 1868-1905, 47 J. Econ. Hist. 379 (1987) (arguing that the prohibition on tontine insurance policies was probably unnecessary).

190. By 1950 the labor force participation rate of men age 65 and older had dropped to only 46%, from the 65% to 70% typical for the pre-Social Security period. It was the period of greatly expanding Social Security and pension benefits in the post-War era that saw the greatest drop in labor force participation by older Americans, so that by 1990, the labor force participation rate for men age 65 and older had dropped to 16%. See James H. Schulz, The Economics of Aging 64-65 (6th ed. 1995).

be rescued by the Social Security system, is too simplistic.\textsuperscript{192}

The innovation of advanced industrial society that began with Social Security was more likely the \textit{presumption} of retirement for all workers upon attainment of a specific age without any demonstrated diminution in ability to work.\textsuperscript{193} Industrialization created both the social wealth that made retirement possible and the risk of extreme levels of unemployment and poverty in old age that prompted enactment of Social Security.\textsuperscript{194} The redistributive aspect of the Social Security entitlement played a key role in the democratization of retirement in the wake of cyclical economic downturns.

The major underlying principle and purpose of social insurance in the United States was very similar to the purpose of the Civil War pension system as it evolved: to prevent, rather than to relieve, poverty in old age for those elderly men and their families who were deemed worthy of public protection. These included veterans and their families under the Civil War system and long-time industrial workers and their families under Social Security.\textsuperscript{195} In this evolving American entitlement structure, the provision of old-age benefits was intended as a prophylactic for poverty—not a remedy for those already in need but a way of preventing the descent into poverty that might, although not necessarily would, accompany old age without work.

The innovative feature of the Social Security program was the redistributive benefit in the context of a mandatory program financed with worker contributions. In essence, Social Security was structured to eventually eliminate the need for explicit needs-based poverty programs by providing weighted benefits to low-wage workers as a matter of earned right.\textsuperscript{196} Within the framework of an expansive democratic capitalist ideal, the authors of Social Security based their approach to income security on the assumption—to which they firmly adhered even in the depths of the Great Depression—that economic rights based on earnings would eventually accrue to all members of society who would either be workers or dependents of workers in a family relationship.

The entire structure of retirement income sources in the

\textsuperscript{192} See Carter & Sutch, \textit{supra} note 177, at 6-11.
\textsuperscript{193} See \textit{id.} at 8-9.
\textsuperscript{194} See \textit{id.} at 7.
\textsuperscript{195} See discussion \textit{infra} Part IV.C.
\textsuperscript{196} See discussion \textit{infra} Part IV.C.2.
United States is based on individually-earned entitlements, proportional to earnings during a worker’s life, that ensure the expectation of income in old age and encourage retirement. Since a strictly proportional structure would provide little assurance of adequate income for moderate- and low-wage workers into a lengthy old age, redistribution was an inevitable and necessary part of a system of prospective public entitlement, intended to both encourage and support retirement without reliance on poor relief for the vast majority.

The combination of private entitlements to future income in old age—such as individual annuities and insurance as well as employer-provided pensions—with the public entitlement of Social Security resulted in a system of individual rights to accumulate as much or as little retirement income as fortune or choice would allow. The earned entitlement, under the American system, was the opportunity to accumulate. The guarantees were not to any level of income but rather to payments from specific sources, which might amount to adequate, inadequate, or even excessive income, but which were designed to avoid imposition of adequacy measures from external authority.

Employers, intensely cost conscious and generally suspicious of centrally imposed payroll burdens, saw the Social Security program as simply another type of employer-provided pension with an employee contributory element. The few business leaders who originally supported Social Security viewed it as a vehicle for relieving employers of pension liabilities they would otherwise be required to shoulder individually in order to make retirement a viable means of easing older employees out the door. The exigencies of the Depression era may have required a collective federal response to destitution—threatened or current—among the elderly; from the perspective of the employer, however, the social insurance portion of the Social Security Act seems to have represented more of a government-managed contributory pension than a broadly based social entitlement.

While it may not have been the primary focus of those designing the legislation, Social Security represents in part a social engineering effort to free up jobs for younger workers by inducing older workers to retire. Clearly such an inducement could not be

197. See discussion infra Parts IV.B.3., IV.C.2.
199. See generally id. at 181-214 (questioning the motives of those implementing
widely successful for the low-wage workers most in need of employment without some redistribution of income through the retirement benefit promised under Social Security. Nonetheless, the conservative structure of Social Security ensured that benefits would not provide a complete retirement income and that workers would still need to provide for themselves in retirement through savings and pensions. The role of private pensions and savings in capital formation, an issue that has taken on primary importance in the debates of the 1990s, was always an important consideration for employers, if not for employees.

It is hardly surprising, then, that any attempts to regulate the

Social Security and suggesting the motives were not completely humanitarian, but rather, utilitarian in nature; see also MYLES, supra note 100, at 11-13 (asserting that managers attempted to institutionalize retirement in order to control the flow of the labor force).

Retirement would open up promotion opportunities for younger workers, thereby enhancing morale; skilled workers could be replaced more readily by the unskilled or by those with the new skills required by changing technology; and, where wages were linked to seniority, highly paid older workers could be replaced by less expensive younger workers.

MYLES, supra note 100, at 13. But see ACHENBAUM, supra note 122, at 106-08. Achenbaum argues that Congress and many advocates of the elderly rejected proposals to require recipients to cease work in order to receive benefits.

The bill submitted by the Committee on Economic Security included a provision drafted by its general counsel, Thomas Eliot, stating that “no person shall receive such old-age annuity until ... not employed by another in a gainful occupation.” Middleton Beaman, legislative counsel to the House of Representatives, objected to this requirement because he thought it would be too difficult to administer. As a result, the House Ways and Means Committee did not stipulate that one retire in order to qualify for an annuity. After hearing additional testimony, members of both houses concurred that Title II of the 1935 Social Security Act should not serve as a compulsory retirement mechanism. Because old-age insurance was to replace income “lost” because of retirement, however, the Social Security Board was authorized to regulate the withholding of pensions from those who “received wages with respect to regular employment.”

Id. at 107 (footnote omitted). This regulatory permission was transformed into the still applicable Social Security “retirement test”. See id. “The ... 1939 amendments ... set a limit on how much a person could make each month and still receive a pension.” Id. While Achenbaum sees this debate as evidence that Social Security's stated purpose was not to induce older workers to retire, the fact that the original version of the 1935 Act went beyond encouragement to coercion seems to support Graebner's view that encouraging retirement to free up jobs for younger workers was at least a subtext for the New Deal support for old-age pensions.


201. See MUNNELL, supra note 46, at 93, 169.
tax benefits, which eventually began to accrue to sponsors of pension plans, should credit employers with "paying" for their workers' Social Security benefits, however inconsistent integration might have been with Social Security's redistributive purpose. The roots of the Social Security benefit entitlement, including its income redistribution, are more deeply embedded in the history of American treatment of the poor and elderly than is the relatively recent recognition of a "right to vested private pension benefits." Nonetheless, an examination of the origins of Social Security reveals a lack of public and employer understanding of the redistribution that was buried in the benefit formula and that would be abrogated by integration of private pensions with Social Security.

A. The "Social Problem" of Aging

The question of poverty and old age as "twinned" phenomena appears to have surfaced first in Europe from at least the period of establishment of compulsory workingmen's insurance programs in Germany in the 1880s. Many of the early American and European social welfare theorists and activists portrayed industrialization as a cruel process that forced older workers into inactivity and poverty. Certainly in contrast to the largely agrarian work setting that dominated American life until after the Civil War, industrial workers were more likely to grow old without recourse to a family farm or homestead, which could provide support and housing, and more likely to rely on continuing family wage income in case of unemployment or disability—whether from old age or misadventure.

Yet the enactment of workingmen's insurance programs in Germany, and elsewhere in Europe, in the 1880s and 1890s appears to have had as much to do with management of an industrial work force as with alleviation of poverty in old age. When

204. See Haber, Over the Hill, supra note 187, at 96-100.
205. See Gratton, supra note 171, at 46.
206. See Gordon, Business, Labor, and Politics, supra note 35, at 120-49;
European nations, as well as Australia and New Zealand, considered the “problem” of old age in the wake of early-twentieth-century industrialization, the solutions were primarily variations on a “top-down” social engineering approach, with the aim of guaranteeing a level of income for the aged through needs-based, citizenship-based, or work-based pension programs.  

From the 1880s through the first decade of the twentieth century, Germany, Britain, Denmark, and other western nations established a variety of social spending programs, some based strictly on need, others on the insurance model for wage workers. The European systems followed two models with complementary but not identical purposes—(1) contributory workingmen’s insurance and (2) noncontributory old-age pensions. Contributory programs were based on the concept of forced savings that would fund life annuities, a centuries-old private insurance concept now adapted to a public context; they were not based on need and were seen as more or less pure insurance against loss of earning capacity due to old age or disability. Contributory programs were also limited in scope, with compulsory contributions levied on wages up to a certain level and coverage of only certain categories of workers.

European noncontributory old-age pensions, such as the programs adopted in Denmark in 1891 and in Britain in 1908, were more explicitly designed to relieve poverty of the current elderly population. These pensions were not tied to work histories and are more properly viewed, especially the British program, as universal old-age income maintenance that would replace the old

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Graebner, supra note 12, at 120-49; Haber & Gratton, Search for Security, supra note 100, at 88-115; Ransom et al., supra note 170, at 77.

207. See Hennock, supra note 203, at 109-215; see also Orloff, supra note 100, at 13-16 (discussing the “late” adoption of welfare programs by Canada and the United States).

208. See Orloff, supra note 100, at 14; see also Hannah, supra note 88, at 15-17 (describing the formation of national pension and insurance programs in Great Britain during the early part of the twentieth century).

209. See Orloff, supra note 100, at 13.


211. According to Skocpol, even by 1910, over 20 years after the imposition of mandatory wage contributions in Germany, only 52% of working Germans were covered by the program with either current or prospective pensions, and most of the pensions then being paid were for disability, not old age. See Skocpol, Protecting Soldiers, supra note 100, at 131-32.

212. See id.
English Poor Laws for the elderly. In contrast to the European pattern, the American experience saw the development of individual annuities and employer-provided pensions to at least a limited extent well before the general employment-based system of Social Security was put in place in 1935. Perhaps in part because the Civil War pension system continued to pay benefits well into the second decade of the twentieth century, demand for social insurance was not strong enough to induce passage of Social Security until the economic crisis of the 1930s.

B. Private Pensions: Labor Management, Industrial Social Welfare

Private pensions have never been the principal or even major source of income in old age for United States workers. Nonetheless, limited pension and profit sharing plans existed in the United States long before the federal retirement program was pushed through the New Deal Congress in 1935. Employer-sponsored group savings plans, and eventually pension plans, seem to have been an outgrowth of the “private social welfare” efforts begun in the late-nineteenth century by American businesses as employers began to perceive the advantages of pension trusts and stock purchase plans, first as a source of capital and later as a way of easing their older and more highly paid employees off the payroll.

While there were a few American business leaders who supported the transformation of employer-provided “industrial welfare” into a broader public program for which the federal government would be responsible, employers generally preferred private employer-provided pensions to government-imposed pensions.

213. See HANNAH, supra note 88, at 15-17; see also HENNICK, supra note 203, at 118-20 (discussing how large a proportion of the population was forced to turn to the Poor Law in old age and how this proportion affected the political arena); MYLES, supra note 100, at 16 (describing the origins of the modern welfare state and illustrating how pre-war public pensions were a form of social assistance for the indigent rather than a retirement wage for the elderly).
214. See discussion infra Part IV.B.
215. See ORLOFF, supra note 100, at 98.
217. See Ransom et al., supra note 170, at 11-19.
218. Marion Folsom, an executive at Kodak who was instrumental in setting up Kodak’s employee benefits programs in the early part of the century, is an example of this not very widespread support. See Sanford M. Jacoby, Employers and the Welfare State: The Role of Marion B. Folsom, 80 J. Am. Hist. 525, 526-27 (1993).
Employer-provided pensions were a valuable tool for employee management while still not committing the employer to promises the company might not be comfortably able to fulfill when workers actually began to retire. Employers appear to have focused on immediate cost, not on long-term retirement behavior, in establishing pension plans, and the history of private employer-provided pensions through the 1930s gives abundant evidence that a private system alone would not give enough workers advance assurance of income in old age to make retirement a mass phenomenon.

1. Extent of pension plan coverage prior to the 1930s

Private employers in the United States began establishing annuity pension plans for their employees late in the nineteenth century, years before the enactment of the federal income tax and the possibility of sheltering income from tax through deferring compensation. The first United States pension plan appears to have been established by the American Express Company in 1875 when American Express was principally associated with the railroad industry. The plan was not a true retirement plan, but rather paid benefits to disabled employees who had twenty years of service with the company, had reached age sixty, and were recommended for the pension by company management.

This type of plan was put into place by many United States and Canadian railroads in the years following 1875, but those plans seem to have been more a response to the occupational hazards presented by railroad employment than an anticipation of retirement pensions. However, most developed into straight retirement plans during the 1900 to 1930 period when the greatest number of industrial pension plans were established. The most widely accepted estimate of pension plans and participation is that between 1875 and 1929 around 400 industrial pension plans were established, with about that number still in operation on the eve of

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219. See Orloff, supra note 100, at 179-80; Ransom et al., supra note 170, at 16-17.
220. See discussion infra Part IV.B.3.
221. See DAN M. MCGILL, FUNDAMENTALS OF PRIVATE PENSIONS 16-17 (3d ed. 1975).
222. See GREENOUGH & KING, supra note 216, at 27.
223. See id. at 27-28.
224. See id. at 30.
225. See id.
the Depression.\textsuperscript{226}

The companies establishing these plans employed about 10% of the industrial labor force—a force substantially less than the entire work force including agricultural and casual labor. It is not clear, however, how many of those employees were eligible to participate in the plan or would eventually qualify for benefits.\textsuperscript{227} According to a recent estimate, although industrial pensions were not uncommon by 1935, no more than 4% of male workers and 3% of female workers met the requirements for receipt of pensions at that time.\textsuperscript{228}

2. Nature of the private pension “right”

Most early pension plans were noncontributory. That is, the plans were financed completely by the employer who generally interpreted the obligation to pay benefits as voluntary.\textsuperscript{229} Perhaps the earliest case exploring the nature of the promise made to the employee in an industrial pension plan was\textit{McNevin v. Solvay Process Company},\textsuperscript{230} in which the court analyzed pensions on the theory that they were a gift from employer to employee.\textsuperscript{231} In that case the ruling turned on the authority of the company’s directors to refuse to pay a pension claim under the plan.\textsuperscript{232} Since the pension payment itself was viewed as a gratuity, there was no automatic obligation to pay even though an amount was “credited” under the employee’s name in the bookkeeping for the plan.\textsuperscript{233}

The “gratuity” theory of pensions matched employer views of their obligations under pension plans at least until after the inception of the income tax\textsuperscript{234}—the plans were written to be strictly discretionary, with payments made out of current income and usually no advance funding for future obligations. Another early case decided a year or two after\textit{Solvay Process} reinforced the gratuity theory by holding that the employer had created no implication of

\textsuperscript{227} See id.
\textsuperscript{228} See Gordon, \textit{Business, Labor, and Politics}, supra note 35, at 247.
\textsuperscript{229} See Greenough & King, supra note 216, at 34-35; see also Quadagno, supra note 100, at 86 (discussing the voluntary nature of noncontributory pensions and employers' disclaimer of any binding obligation to provide benefits).
\textsuperscript{230} 53 N.Y.S. 98 (1898), \textit{aff'd per curiam}, 60 N.E. 1115 (N.Y. 1901).
\textsuperscript{231} See id.
\textsuperscript{232} See id. at 100.
\textsuperscript{233} See id. at 99-100.
\textsuperscript{234} See id.
employee vesting in amounts credited under employee names and that upon the bankruptcy of the employer, the employees had no rights as creditors.\textsuperscript{235} Even though these cases found no legal entitlement and no employee vesting in the absence of a plan provision specifically providing for it, employers nevertheless stopped the practice of crediting amounts to employee bookkeeping accounts for fear of creating any possible admission of liability under the pension plan.\textsuperscript{236}

While the gratuity theory was cited by the courts well into the 1950s,\textsuperscript{237} in the 1920s some courts apparently began to uphold employee claims on noncontributory funds on the grounds that the pension was part of a contractual agreement between employer and employee, not simply a gift.\textsuperscript{238} Perhaps as a result, employers began to cut back on noncontributory plans: "After 1923, new pension plans were overwhelmingly contributory and insured, and many employers pared back their programs or simply stopped notifying workers or their dependents of pension eligibility."\textsuperscript{239}

3. Growth and retrenchment of the private retirement solution

The modest expansion of employer-sponsored pension plans from 1900 into the 1920s coincided with increasing use of labor management practices designed to limit employee turnover and fend off union organization.\textsuperscript{240} Unions in general opposed establishment of employer-provided plans. They viewed the plans as an interference with bargaining rights although they occasionally set up their own benefit plans, frequently covering sickness, disability, and unemployment, and less frequently old age, payable only if sufficient funds were available.\textsuperscript{241}

\textsuperscript{235} See Dolge v. Dolge, 75 N.Y.S. 386, 387-88 (Sup. Ct. 1902).
\textsuperscript{236} See GREENOUGH & KING, supra note 216, at 38.
\textsuperscript{237} See W. E. Shipley, Annotation, Rights and Liabilities as Between Employers and Employee with Respect to General Pension or Retirement Plan, 42 A.L.R.2d 461, 464-67 (1955).
\textsuperscript{238} See QUADAGNO, supra note 100, at 92.
\textsuperscript{239} GORDON, BUSINESS, LABOR, AND POLITICS, supra note 35, at 254; see also QUADAGNO, supra note 100, at 91-95 (discussing the major shift to contributory plans in 1925).
\textsuperscript{240} See QUADAGNO, supra note 100, at 80-91; see also GORDON, BUSINESS, LABOR, AND POLITICS, supra note 35, at 248-50 (discussing the tendency for companies to view pensions as weapons against turnover and unionization).
\textsuperscript{241} See GORDON, PITIED BUT NOT ENTITLED, supra note 23, at 248 (referring to "if and maybe" pensions); see also GREENOUGH & KING, supra note 216, at 40-41 (stating the earliest aid activities of trade unions focused on more immediate needs and not old age).
Employers saw pension plans as a means to an end: workers would trade a pay increase or right to strike for the promise of a pension. Moreover, pensions could be used to "purge the payroll" of older workers who were probably more highly paid and had begun to be perceived as less productive. Since the pension promise itself was so tenuous and required no current funding or payment of benefits except to those who retired immediately after a plan was established with benefits substantially lower than their salaries had been, current employment costs theoretically could be reduced along with turnover of valued employees. Stock purchase plans were even more narrowly focused to accomplish specific business goals—to raise capital and reinforce employee identity with the aims of the company as opposed to with unions—and appear to have had little to do with providing for employee retirement income.

The very modest use of employer-provided pensions coincided with other labor management practices such as seniority, a fact that both aided and impeded older workers. Workers who "caught on" with a company when they were relatively young could benefit from seniority practices that gave preference in sal-

242. See GRAEBNER, supra note 12, at 131-32. Graebner cites Frank Vanderlip, of the National City Bank of New York, in an article published in 1905 as promoting noncontributory private pension plans as valuable in controlling a work force. See id. at 131. "For the sake of a pension an employee would, he believed, 'sacrifice much of his personal liberty, including his right to strike for better wages or shorter hours.'" Id. at 131-32; see also QUADAGNO, supra note 100, at 81-85 (giving examples of "misconduct rules" that employers could use to revoke pension rights).

243. See GORDON, BUSINESS, LABOR, AND POLITICS, supra note 35, at 248; GRAEBNER, supra note 12, at 121-29 (discussing the function of retirement as a way to rid the workplace of older people).

244. See GORDON, BUSINESS, LABOR, AND POLITICS, supra note 35, at 248-49. Retirement of older employees, at least in the first years of a plan, reduced payrolls because replacement wages were substantially lower or positions were not filled. At Kodak, pensions were introduced as a means of flushing out the "privileged senility" and "deadweight" of older workers, and half of pensioned employees were not replaced. At the Pennsylvania Railroad, redundancy ran at about one-third, "showing a distinct saving to the company." In a detailed survey of 302 workers pensioned at DuPon in 1923 and 1930, 39 positions were scrapped, 89 were divided among existing employees, and 180 were filled by new hires; for those years at least, savings ran at $200 per pensioner. Such economies were far from universal and became difficult to sustain as pension rolls grew. Indeed, the payroll-savings argument was often simply a board-room rationale for a plan aimed at turnover and the retention of skilled workers . . .

245. See id. at 248 (footnote omitted).

246. See HABER & GRATTON, SEARCH FOR SECURITY, supra note 100, at 108-09.
ary and job protection to longer-service workers. Henry Ford's innovation of the wage ladder, an artificial hierarchy of pay based on length of service that encouraged workers to stay with the company, was just one example of the many kinds of employee benefits, including pensions, that were increasingly tied to longevity after 1900. The seniority system probably worked to the disadvantage of those older workers attempting to find new employment in middle age, since they could not offer a long period of service and high youthful productivity, characteristics that seniority and benefit plans were developed to encourage.

The concept of mandatory retirement took hold in American business during this period as well, particularly in industries such as the railroads, which had already established employer-provided pensions and organized their compensation and benefits around longevity of employment. In 1900 the Pennsylvania Railroad established a maximum hiring age of thirty-five and retirement age of seventy, with a company pension, as a way of controlling the costs of expensive older workers while at the same time reducing employee turnover.

Of course, pension promises that appear quite inexpensive when made often turn out to be much more expensive when they actually have to be fulfilled. While employers limited the likelihood of eligibility for pensions with long service requirements and requirements that the worker be employed at the time of disability or retirement, pension liabilities still became a major cost issue for employers in the late 1920s:

Firms found welfare costs, although averaging only 2 percent of payroll, increasingly burdensome. Pension liabilities ballooned with each year's retirement, unanticipated expenses and legal awards continued to rankle, and administrative and benefit costs grew steadily. . . . Welfare capitalists had anticipated neither spiraling costs and liabilities nor the advantages reaped by competitors without welfare obligations. . . . The [National Industrial Conference Board] noted that "many companies found

247. See id. at 106-09.
249. See Haber & Gratton, Search for Security, supra note 100, at 195 (discussing the likelihood of retirement for older workers in the industrial era).
250. See Latimer, supra note 226, at 22-26, 99-100.
251. See id. at 24-25.
themselves seriously embarrassed by their pension obligations,” and the [Special Conference Committee] thought it “unlikely that the ill-considered liberality of some of the older pension plans will ever be repeated.” From 1928 to 1931, aggregate pension costs increased by 50 percent and liabilities swelled to over $2 billion.252

Many employers in the 1920s attempted to mitigate the impact of these rising costs by insuring their pension liabilities, but even the insurers began to be alarmed by the size of future costs.253 An employer group conference in 1925, held to discuss the “funding crisis” of private pension plans, proved to be a forum for large insurance companies to lambaste employers for making ill-considered and costly pension promises that they would not be able to fulfill.254 Yet the cost of insurance premiums to cover those pension promises appeared to be equally expensive, and many employers resisted the insurance option—“a resigned majority hoped to spread the costs . . . by ‘making [pension] plans compulsory throughout industry as rapidly as it was practicable.’”255

Thus, even before the advent of the deep economic crisis in the 1930s, companies were attempting to retrench on retirement commitments they had already made. Some larger employers, perhaps recognizing the link between seniority, employee management, and retirement income, began to support calls for federalization of retirement programs.256 Most businesses, however, resisted any suggestion of federal intervention and instead continued to cut back on plan promises.257

This brief history reveals the limited aspirations of employer-sponsored private pension plans in the pre-World War II era. The goal of most employers was control of their labor forces, not retirement income security. Funded plans were seen as vehicles for capital formation, not income replacement in old age. The con-

252. GORDON, BUSINESS, LABOR, AND POLITICS, supra note 35, at 253-54. The National Industrial Conference Board and the Special Conference Committee were organizations of large employers founded in 1916 and 1919, respectively. See id. at 147-59.
253. See id. at 255.
254. See id.
255. Id. (quoting John Raskob).
256. See GRAEBNER, supra note 12, at 184-87 (discussing support from an advisory counsel consisting of representatives from Eastman Kodak, Standard Oil, and General Electric); Jacoby, supra note 218, at 538-40.
257. See GORDON, BUSINESS, LABOR, AND POLITICS, supra note 35, at 253-57.
tinuing pressure from workers for pension plans, and their willingness to accept an extremely insecure pension promise as a tradeoff for current wages, reflects the general insecurity created by industrialization and dislocation of traditional trade occupations. Nonetheless, private pension plans, which were almost always unfunded and benefited almost exclusively long-term—thirty years or more in many cases—high-wage workers, could not be expected to, and did not, underwrite mass retirement as shown by the continued high labor force participation rates of both male and female workers over age sixty-five up until the inception of Social Security.\textsuperscript{258}

\textbf{C. The Federal Response: Social Insurance—Redistribution for the Worthy}

The United States did not put in place a federal working person’s insurance or old-age pension program of a scope comparable to European systems until the Social Security Act of 1935.\textsuperscript{259} Part of the need for government response to the possibility of poverty among elderly workers was met, as discussed above, by the Civil War pension program, which paid out benefits that were similar in percentage of the number of elderly paid, and higher in amounts paid, to the European systems at least until the decade following 1910.\textsuperscript{260} But the establishment of a federal public old-age pension program, whether contributory or noncontributory, had to wait until the Great Depression created both a very real spectre of widespread poverty among the elderly—and future poverty in old age for younger workers—and a perceived need to encourage retirement and free up jobs for younger workers.

Even though private pensions failed to prevent old-age poverty for workers in the wake of the widespread economic disaster of the 1930s, it was natural at the inception of public social insurance in the United States to think of the Social Security program as essentially similar to the European model of prepaid worker’s annuities, a type of forced savings for the working and middle classes. The fact that private pensions and annuities were the precursors of public social insurance aimed specifically at the elderly had a formative effect on the way Social Security was perceived by both workers and employers and on the provisions of the statutes.

\textsuperscript{258} See supra note 179 (discussing labor force participation rates).

\textsuperscript{259} See GRAEBNER, supra note 12, at 15 (stating that burdens of old-age assistance were first transferred to the federal government in 1935).

\textsuperscript{260} See discussion supra Part III.B.2.
enacted in 1935 and 1939.

Yet the federal program was never intended to be the sole or major support for retired workers even as the Social Security program matured—benefits were designed to replace on average only about 45% of the pre-retirement earnings of a worker with average earnings over a lifetime of one-half the maximum wage base.261 One question then is how, if at all, the framers of the Social Security Acts of 1935 and 1939 intended private pensions to be coordinated with Social Security retirement benefits.

While there is no direct discussion of coordination in the legislative history of Social Security, the possibility of covering under Social Security only those workers without private pensions was specifically rejected by the drafters of the original and subsequent Social Security acts.262 Compulsory coverage was a cornerstone of the legislation, and universal coverage of all workers was the goal of most of the original designers.263

Since the enactment of Social Security preceded the tax regulation of employer-provided pensions inaugurated in 1942, there was apparently no contemplation of the inverse possibility, created by the integration provisions, that workers covered by Social Security might be deprived of their private pensions. The rejection of partial or voluntary coverage under Social Security, along with the rejection of means-testing and the emphasis on earned entitlement, was consistent with the structure of entitlement developed in the Civil War pension system—pensions based on worthiness were a source of income to be augmented, not replaced, by private means.

1. The Great Depression and the threat of old-age insecurity

As the economy began to spiral downward in the late 1920s and early 1930s, American workers relied on a patchwork of resources to provide for income should they no longer be able to work in old age. A few, certainly no more than 5%, had private pension plans on which they might rely; many had savings of at least modest amounts; and some, mostly the middle-and upper-middle-class professionals, had private annuities.264 The various railroad company pension plans developed into a nationwide co-

261. See Myers, supra note 34, at 361-65.
262. See Brown, supra note 80, at 57-59.
263. See id. at 57-70.
264. See Ransom et al., supra note 170, at 4-5.
ordinated system for all railroad workers, and most government employees had civil service pensions, state or federal, that were designed to provide fairly complete retirement income.\textsuperscript{265} Probably as or more important than formal pension arrangements was the network of family resources that provided assurance to older workers who lost their jobs or were involuntarily "retired" that their children could help out with income and housing if necessary.\textsuperscript{266}

All of these resources came under severe attack and many simply collapsed as the economy contracted after the stock market crash. Between 1929 and 1932, forty-five private plans covering one hundred thousand workers were terminated, and many employers used accumulated pension trusts to cover other obligations, never paying benefits owed to their employees.\textsuperscript{267} The railroad plan was close to bankruptcy even before the Depression because of the increasing numbers of retirees and declining railroad revenues to support the system through payroll withholding, necessitating a federal rescue plan that presaged enactment of Social Security.\textsuperscript{268}

But the threat to formal pension arrangements paled in comparison to the simple, overwhelming facts of massive unemployment and plummeting asset values.

The scale of the downturn defies easy description. From the crash of late 1929 to the trough of 1932 . . . . [n]ational income plummeted 40 percent, wages fell over 60 percent, and real weekly earnings (despite deflation) dropped from $25.00 to barely $20.00 . . . . National unemployment, which reached 25 percent by 1933, paled beside joblessness in core industry centers: 50 percent in Cleveland, 60 percent in Akron, 80 percent in Toledo. In the West and South . . . . [a]verage annual farm incomes fell from a pre-1929 average of $1,000 to barely $300 by 1932,
and banks foreclosed nearly 1,000,000 farms between 1930 and 1934. 269

Even those who had saved for possible retirement or as a hedge against unemployment were not secure in the face of the Depression, as one-fifth of the nation's banks failed, taking the savings of nine million families with them. 270

A complete discussion of the impact of the Great Depression on income and retirement is beyond the scope of this Article, and the competing theories as to the economic and political roots of Social Security are laid out in a variety of recent studies. 271 It is possible, however, to identify selected aspects of the Depression as pivotal influences on the development of public and private retirement income entitlements from 1935 onward.

First, unemployment, bank failures, and declining property values probably disproportionately affected the accumulated capital or property intended as sources of future income security for both young and middle-aged workers in old age. Moreover, as unemployment deepened and reached more middle-class workers, even those older workers who had held onto their jobs through seniority systems began to be laid off. 272 Their options for returning to work were very limited in 1935, and the unemployment of the children of older workers meant that whole families were no longer able to provide sufficient household income to support elderly dependents. 273

Thus, the possibility of insecurity and poverty in old age, even for those who had worked their whole lifetimes, was as important as the reality. Younger workers saw grim prospects for themselves as declining wages made even limited savings impossible and private retirement arrangements failed. Into the mid-1930s, unemployment for older workers climbed dramatically, and they faced permanent unemployment with few alternative income sources. 274

269. GORDON, BUSINESS, LABOR, AND POLITICS, supra note 35, at 160.
270. See HABER & GRATTON, SEARCH FOR SECURITY, supra note 100, at 42.
271. See id. at 95-110, 122-42; Gratton, supra note 171, at 416; see also EDWARD D. BERKOWITZ & KIM MCQUAID, CREATING THE WELFARE STATE: THE POLITICAL ECONOMY OF 20TH CENTURY REFORM 1-2, 7 (1992) (discussing the impact of the private sector on the creation of the American welfare state); GRAEBNER, supra note 12, at 162-63 (discussing the ideology of social security evolving from concern for the needs of older workers); ORLOFF, supra note 100, at 7 (discussing the imposition of old-age pensions throughout Britain, Canada, and the United States).
272. See HABER & GRATTON, SEARCH FOR SECURITY, supra note 100, at 165.
273. See id.
274. See id. at 110.
The severity and longevity of economic disaster in the 1930s closed off both work and self-sufficient retirement options for older workers, presenting an example of the economic insecurity younger workers had to look forward to when they themselves reached old age.

Second, the collapse of private pensions and the disappearance of personal savings in bank failures must have aptly conveyed to ordinary people the fragility of private entitlements. Even pension plans, which gave workers a vested right to benefits, were unable to fulfill their obligations as companies went bankrupt, and it seems unlikely that even advance funding would have made a difference in light of the stock market collapse. The combination of mass unemployment with the loss of accumulated savings and pensions meant that individual effort could very well prove insufficient to maintain one’s economic position or to stave off poverty when old age brought increasingly likely unemployment.

It is frequently observed that the scale of economic disaster during the Depression prompted a national, federal poor-relief effort, of which the Social Security Act, with both its social insurance and direct poor-relief assistance features, was the final expression. The reorganization of the work force is less frequently cited as a major effect of the Depression, but clearly the modern institution of age sixty-five retirement began with the initiation of Social Security old-age benefits in the 1935 Act.2


The Social Security program was enacted in two major legislative efforts of the New Deal: the Social Security Act of 1935277 and the substantial revision enacted by the Social Security Amendments of 1939 (1939 Act),278 which expanded coverage and benefits and accelerated the first payment of Social Security benefits from 1942 to 1940. The stated purpose of both the 1935 Act and the 1939 Act was “preventing dependency in old-age”; the goal of the contributory Social Security program was to “enable

275. See, e.g., GORDON, BUSINESS, LABOR, AND POLITICS, supra note 35, at 268-69; HABER & GRATTON, SEARCH FOR SECURITY, supra note 100, at 81-87; KATZ, supra note 23, at 206-34.
276. See HABER & GRATTON, SEARCH FOR SECURITY, supra note 100, at 88-89, 110-11.
277. See BERKOWITZ & MCQUAID, supra note 271, at 106.
younger workers, with matching contributions from their employers, to build up a more adequate old-age protection than it is possible to achieve with noncontributory pensions based on a means test. At the time, the Committee on Economic Security estimated that out of 6.5 million people over age sixty-five in the United States, only 150,000 aged people were receiving "industrial and trade-union pensions," with possibly an equal number receiving veterans' or public retirement system pensions.

While these purposes are widely accepted as accurately reflecting at least part of the impetus for Social Security, historians disagree as to how much the process of formulating and passing the Social Security Act was influenced by private employers wishing to shift their pension liabilities onto the federal government. It is also unclear how deliberate New Deal reformers were in designing programs to pull older workers out of the labor market in order to free up employment for younger workers. However, whether or not the drafters of the Social Security Acts intended to create the expectation of retirement at age sixty-five, it is clear that the existence and later expansion of Social Security had that effect.

The basic features of Social Security were all part of the original 1935 Act: compulsory coverage with no ability to "opt out" for those covered by private pensions—despite considerable discussion of that alternative; no means-testing of benefits; a benefit formula based on past earnings and weighted in favor of lower-paid workers; and a financing scheme that assessed equal percentages of tax—called "contributions"—on employers and employees

280. See id. at 44.
281. See, e.g., Gordon, Business, Labor, and Politics, supra note 35, at 279 ("[T]he Social Security Act passed in 1935 was largely the work of a motley coalition of business interests grasping for solutions to the ravages of economic competition and federated economic regulation."); Quadagno, supra note 100, at 99 (Social Security represents a tool of industrial capitalism for controlling and rationalizing its labor force). But see Achenbaum, supra note 122, at 18-37 (arguing that the New Deal reformers did intend to establish a form of welfare state but had to adopt conservative "insurance" terminology and provisions for political reasons); Theda Skocpol & John G. Ikenberry, The Road to Social Security, in Theda Skocpol, Social Policy in the United States: Future Possibilities in Historical Perspective 147-56 (1995) (emphasizing the role of a fractured political structure in the United States which allowed Wisconsin social theorists to have an influential role in formulating the federal Social Security program in a country which otherwise resisted European-style welfare state programs, leading to a patchwork of programs for the deserving elderly—Social Security—and unsupported programs for the poor).
282. See Haber & Gratton, Search for Security, supra note 100, at 111.
up to the taxable wage base set at $3000 per year where it remained until 1951.\textsuperscript{283} Expansions in coverage of workers and in categories of beneficiaries—for example, dependent spouses and children—were made in 1939 and after World War II,\textsuperscript{284} but the essential old-age pension entitlement was intact from the beginning.

All of these features were of critical importance in creating a program intended to prevent future dependence in old age for those attached to the work force for all or most of their adult lives. The continuity with Civil War pensions, as well as the distinctions from the older program, were clear: the group deemed worthy of public entitlement was expanded from former soldiers to all those working in paid employment, while the condition triggering payment of benefits was attainment of old age—essentially the point to which the Civil War pension system had evolved by 1900.\textsuperscript{285}

The Depression created the conditions necessary for broad public support for an age-based public entitlement, but the key elements of that entitlement were all designed to underwrite mass voluntary retirement in the future, not to address the massive poverty created by the economic dislocation of the 1930s. The essential characteristics of Social Security have not significantly changed: prospective redistribution built into the benefit formula based on the past working lifetime rather than on current poverty; coverage of workers regardless of their participation in employer-sponsored pension plans; financing by both employers and employees that, despite the annuity-financing rhetoric of the time, was not related to specific levels of individual benefits; and benefit entitlement based on earnings history, not need at the time of retirement.

Even though the dual contribution structure was portrayed at the time as being similar to an annuity-financing structure,\textsuperscript{286} the benefit structure from the beginning belied that interpretation—benefit amounts were and continue to be unrelated to the amount of taxes paid. The Social Security benefit has always been a public

\textsuperscript{283} Robert M. Ball, The 1939 Amendments to the Social Security Act and What Followed, in 50TH ANNIVERSARY EDITION REPORT OF THE COMMITTEE ON ECONOMIC SECURITY OF 1935 AND OTHER BASIC DOCUMENTS RELATING TO THE DEVELOPMENT OF THE SOCIAL SECURITY ACT 162-67 (1985) [hereinafter Ball, CES 50TH]; see also Myers, supra note 34, at 229-371 (discussing development of the old-age, survivors, and disability insurance systems).

\textsuperscript{284} See Myers, supra note 34, at 232, 238.

\textsuperscript{285} See discussion supra Part III.B.

\textsuperscript{286} See discussion infra Part IV.C.2.b.
entitlement based on earnings; even though the financing structure for those benefits was always based on employer and employee FICA contributions and accumulated interest thereon, entitlement to benefits is earned independently of whether taxes are actually paid. Nonetheless, the contributory financing scheme undoubtedly helped to convince employers and IRS staff in later years that it was perfectly consistent to allow employers to effectively "count" their FICA payments as part of their contribution for pensions for low-wage employees.

a. social insurance and labor force management

The problem set for the Committee on Economic Security (CES), established by Executive Order on June 29, 1934, "was to study methods of providing 'security against the hazards and vicissitudes of life,' with the primary purpose of developing a workable social insurance system." The CES was headed by Labor Secretary Frances Perkins, and the final report was sent with recommendations to Congress on January 15, 1935.

The CES viewed the situation of older workers in 1934 from the perspective of both the currently old and impoverished who needed immediate assistance and the current worker who required some assurance of security in future old age in light of high and increasing unemployment among workers age sixty-five and older.

289. See Cohen, CES 50TH, supra note 84, at 5-7.
290. See Report, CES 50TH, supra note 79, at 44-45.

The number of the aged without means of self-support is much larger than the number receiving pensions or public assistance in any form. At this time a conservative estimate is that at least one-half of the approximately 7,500,000 people over age 65 years now living are dependent. Children, friends, and relatives have borne and still carry the major cost of supporting the aged. Several of the State surveys have disclosed that from 30 percent to 50 percent of the people over 65 years of age were being supported in this way. During the present depression, this burden has become unbearable for many of the children, with the result that the number of old people dependent upon public or private charity has greatly increased.

... The depression has largely wiped out wage earners' savings and has deprived millions of workers past middle life of their jobs, with but uncertain prospects of ever again returning to steady employment. Employment difficulties for middle-aged and older workers have been increasing, and there is little possibility that there will be a reversal of this trend in the near future.
The CES's recommendations were based on an assumption that men and women reaching age sixty-five would likely live ten to fifteen years longer and that most, if not all of them, would not want to live dependent on charity or family for support as many were at that point forced to do.\textsuperscript{291}

There is no consensus among historians concerning the role of so-called "welfare capitalists"—employers who maintained private pensions and other employee benefits—in the passage of the New Deal in general and of Social Security in particular.\textsuperscript{292} It seems likely that no unified message was delivered to Congress and the administration from businesses demanding a publicly supported retirement program that would relieve them of private obligations.\textsuperscript{293} Nonetheless, some employers saw the advantages of the federal government taking on some responsibility for relief in the face of high and persistent levels of unemployment, particularly as more radical alternatives began to be popularized through the Townsend movement\textsuperscript{294} for old-age pensions.\textsuperscript{295}

At the same time, policymakers in the New Deal administration saw social insurance—along the European model but without open-ended financing—as the answer to several problems. The battles over the details of Social Security are described in detail in several accounts by both the original players themselves and later historians,\textsuperscript{296} but it seems safe to say that earnings-related old-age

\textit{Id.}

\textsuperscript{291} See \textit{id.}

\textsuperscript{292} See \textit{Gordon, Business, Labor, and Politics, supra} note 35, at 269; \textit{Skocpol, Protecting Soldiers, supra} note 100, at 26-28; \textit{Jacoby, supra} note 218, at 526.

\textsuperscript{293} See \textit{Gordon, Business, Labor, and Politics, supra} note 35, at 268-69.

\textsuperscript{294} See \textit{Jacoby, supra} note 218, at 528.

\textsuperscript{295} Marion Bayard Folsom of Kodak appears to be one example, as discussed in \textit{Jacoby, supra} note 218, at 526-27; see also \textit{Gordon, Business, Labor, and Politics, supra} note 35, at 241-42 (discussing the importance of standardizing of welfare costs to employers struggling for market dominance).

Federal welfare law was the logical culmination of a quarter-century battle over the scope and costs of industrial welfare plans and a direct descendant of the anticompetitive business strategies of the 1920s.

\ldots  [E]mployers, pressed by the costs and inconsistencies of private welfare, looked to the states to socialize the resultant financial burden; in turn, inconsistent state legislation compounded the inequities of that burden and encouraged welfare capitalists to look to the federal government.

\textit{Id.}

\textsuperscript{296} See \textit{Report, CES 50TH, supra} note 79 (containing several accounts). J. Douglas Brown gives another account. See \textit{Brown, supra} note 80, at 25-83; see generally \textit{Martha Derthick, Policy Making for Social Security} 5-9 (1979) (discussing the effect of policy "insiders" and professional government staff in for-
pensions were seen only partly as a solution to current old-age poverty and more as a solution to future work force stabilization. The Old-Age Assistance program, the state-run needs-based program for the elderly, paid out more in benefits to more older people from 1936 to 1950 than the social insurance portion of the Social Security Act, and may have had more effect on employment rates among elderly men in that period.

Nonetheless, many New Deal policy specialists specifically foresaw social insurance as the most effective way to induce older workers to retire over the long run, shrinking the labor force to reduce unemployment among younger workers, while providing income transfers to maintain consumption levels into old age. The key features of the social insurance program reflect a desire to ensure younger workers that their working life could be ended based on a guarantee of retirement income, regardless of their financial circumstances when they reached old age. Again, prospective security was the most critical characteristic of the Social Security entitlement if the ultimate purpose was to encourage retirement and social stability in old age. The prophylactic antipoverty function of Social Security was intimately connected to the structure of benefits and financing and was clearly based on an underlying optimism that the economy would eventually provide jobs for all who needed to work up until retirement.

While some alleviation of current need among the elderly became possible as payment of benefits was accelerated to 1940 from the original date of 1942, the entire program was structured in a way designed to assure each generation of workers future security against falling into poverty, not to provide the current generation of elderly relief from poverty. Because of this advance assurance of income once work was no longer possible, available, or desired, retirement became an accepted and expected phase of life, not simply the privilege of the propertied or the feared period of destitution at the end of life for the working poor. The redistributive

297. See HABER & GRATTON, SEARCH FOR SECURITY, supra note 100, at 111-12.
298. See id.
299. See GRAEBNER, supra note 12, at 201-14.
300. Most recent historians have come to this conclusion, with varying emphases on the timing and desirability of mass retirement. See GRAEBNER, supra note 12, at 227-31; HABER & GRATTON, SEARCH FOR SECURITY, supra note 100, at 110-12; SKOCPOL, PROTECTING SOLDIERS, supra note 100, at 525-35. However, the direct connection of earned entitlement, redistribution, and retirement specifically has been little discussed in debates over the best way to alleviate poverty among both
entitlement to Social Security benefits was a necessary precondition for the democratization of retirement.

**b. contributory financing and redistributive benefits in the 1935 Act**

While New Deal reformers emulated the European models of workers’ insurance in many aspects of Social Security, they were wary of open-ended spending on old-age pensions such as had occurred with the many expansions of the Civil War pension system. Many thought that contributory financing, which would provide a limited funding source, would be the best mechanism for insuring that program spending would not repeat the Civil War pension pattern. But limiting total program spending was not the only purpose for the contributory financing scheme—employee contributions were viewed as a key element in creation of the benefit entitlement:

Contributions by the employees represent a self-respecting method through which workers make their own provision for old age. In addition many workers themselves on the verge of dependency will benefit through being relieved of the necessity of supporting dependent parents on reduced incomes, and at the expense of the health and well-being of their own families.

Of course, if it had been literally feasible for workers to “make their own provision for old age” in 1935, there would have been little purpose in establishing a public benefit entitlement. Yet the contributory financing structure clearly seemed necessary to create the entitlement connection even though benefits would be calculated based on earnings.

Under the 1935 Social Security Act that followed the CES’s report, the Old-Age Assistance program, administered by the states, was intended to provide immediate assistance to the elderly who were already poor. The Old Age Social Insurance (OASI) contributory program was intended from the start to provide an earned entitlement and long-term future economic security for the generations that were still working, while providing some future

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301. See SKOCPOL, PROTECTING SOLDIERS, supra note 100, at 532-34.
302. See Report, CES 50TH, supra note 79, at 53.
303. Id.
304. See GRAEBNER, supra note 12, at 191-92.
income redistribution for workers with a lifetime of low earnings.\textsuperscript{305}

A contributory annuity system . . . will enable younger workers, with the aid of their employers, to build up gradually their rights to annuities in their old age. Without such a contributory system the cost of pensions would, in the future, be overwhelming. Contributory annuities are unquestionably preferable to noncontributory pensions. They come to the workers as a right, whereas the noncontributory pensions must be conditioned upon a 'means' test. Annuities, moreover, can be ample for a comfortable existence, bearing some relation to customary wage standards, while gratuitous pensions can provide only a decent subsistence.\textsuperscript{306}


\textbf{\ldots \ldots}

In considering the costs of the contributory system, it should not be overlooked that old-age annuities are designed to prevent destitution and dependency. Destitution and dependency are enormously expensive, not only in the initial cost of necessary assistance but in the disastrous psychological effect of relief upon the recipients, which, in turn, breeds more dependency.\textsuperscript{307}

The benefit structure contemplated by the CES, and ultimately enacted by Congress, was deliberately designed to reflect the working population's income distribution during the working lifetime—that is, benefits would be based on lifetime earnings, thus keeping workers in old age in roughly the same economic position they were in during their working years. Nonetheless, it was necessary to supply workers with very low lifetime earnings a higher level of benefits than strict proportionality would produce. This effort was necessary to meet the ultimate goals of the program—assurance to workers that a long attachment to the work force would ultimately result in sufficient income to support a voluntary exit from the labor force at age sixty-five, regardless of economic downturns resulting in unemployment or devaluation of accumulated savings or assets.\textsuperscript{308}

The original CES plan contemplated a program in which the benefits in the future would be completely financed by worker and

\begin{itemize}
  \item \textsuperscript{305} See Quadagno, supra note 100, at 115.
  \item \textsuperscript{306} See Report, CES 50TH, supra note 79, at 45.
  \item \textsuperscript{307} Id. at 53.
  \item \textsuperscript{308} See Sylvester Schieber, Social Security 20-21 (1983).
\end{itemize}
employer contributions and earnings thereon, somewhat like a defined benefit private pension plan in which definite levels of benefits are promised and financed by sufficient funds that are set aside and invested for that purpose. However, because benefits would begin to be paid out to older workers before benefits were fully funded in advance, the program would inevitably require either advance infusion of general revenues, representing a “funding” contribution for future benefits, or reliance on a “pay as you go” financing scheme. The latter course was chosen:

[Advance funding] would unfairly burden the younger part of the present generation, which would not only pay for the cost of its own annuities but would also pay a large part of the annuities to the people now middle-aged or over. . . . [T]he plan we advocate amounts to having each generation pay for the support of the people then living who are old.\(^{309}\)

Much of the rhetoric surrounding Social Security from 1935 onward was based on its contributory nature—that is, the idea that workers become entitled to benefits based on contributions under the FICA tax system.\(^{310}\) The CES report emphasized the importance of a self-financed system and of benefits based on contributions rather than need or “dependency.”\(^{311}\) However, the entitlement to benefits is in fact based on earnings, not contributions. The contributions are of course also based indirectly on earnings since FICA taxes are a percentage of wage earnings, but the entitlement to benefits is not, and never has been, dependent on whether taxes have in fact been paid.\(^{312}\)

When the original 1935 Act was drafted, the taxation and benefit provisions were placed in separate titles for fear that the Act would be found unconstitutional.\(^{313}\) Thus, it is not clear whether there was a conscious decision to create entitlement based on earnings rather than contributions.\(^{314}\) Nonetheless, the emphasis placed in the report, and in later discussions of the “actuarial

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309. Report, CES 50TH, supra note 79, at 52.
310. See ACHENBAUM, supra note 122, at 35.
311. Id. at 29-32.
312. See BROWN, supra note 80, at 71-83. The Social Security Act entitles benefits to all those meeting insured status requirements through earnings in covered employment. Collection of Federal Insurance Contribution Act taxes is authorized under §§ 3101-3128 of the Internal Revenue Code.
313. See ACHENBAUM, supra note 122, at 18-37; ORLOFF, supra note 100, at 289.
314. See ORLOFF, supra note 100, at 290-91.
fairness" of the contribution and benefit system, on the connection between financing through contributions and benefits ultimately paid can be seen as a secondary argument about the limits of public financing, an argument that obscures the actual structure of Social Security benefit entitlements. Contributions are the concrete representation of the existence of earnings; the employee share of FICA tax is both a financing mechanism and a symbolic representation of the link between earnings and benefits.

Perhaps the most significant difference between the plan proposed by the CES in 1934 and the Social Security Act in 1935 was the expansion of coverage to wages of all workers in covered employment up to $3000 per year. The original plan proposed by the CES was an annuity plan only for very low-wage workers, under which high-wage workers would not have been covered at all in years during which they had more than $250 per month in wages. Under the original plan, therefore, the only income redistribution would have occurred primarily among low-income workers and their employers, as steady high-wage workers would not have been participants. The final legislation's expansion of coverage, and taxation, to all workers and employers in industrial employment, while limiting credit in the earnings history to $3000 per year, meant that the burden of redistribution was spread over all workers in the economy. The system's benefits, however, would always be of limited value as retirement income to workers who maintained lifetime high earnings.

More importantly, this change meant that the system became a true poverty prevention program in that all workers would accumulate earnings credits towards pensions throughout a working lifetime that was likely to include both high and low earnings. Under the original CES proposal, poverty would have been treated as a static condition, assumed to last for the working life of the worker and thus necessitating a public pension program only for the working poor. The revised benefit and financing formula, in contrast, can be seen as reflective of liberal democratic assumptions about economic opportunity and mobility under industrial

315. See Brown, supra note 80, at 71-83.
316. See Report, CES 50TH, supra note 79, at 49.
317. As under current law, benefits were to be calculated only based on covered earnings. Therefore, workers with earnings above $3000 would get no Social Security benefits based on those higher earnings.
318. See generally Schieber, supra note 308, at 20-21 (describing the CES's approach to the Social Security program's benefit structure).
capitalism. Since workers with low earnings in one year may well be workers with high earnings in later years, and vice versa, a true insurance approach should cover all earnings—with or without a wage limit—in order to have a large enough pool to properly spread the risk of low earnings that would be insufficient to secure an adequate retirement income.\(^\text{319}\)

Under this theory, all workers should participate in order to properly spread both the risk of poverty at the end of life and the rights to future benefits over both winners and losers in the economic system. The weighting in the benefit formula that paid proportionately higher benefits to those with low lifetime averages resulted in a benefit structure that would still not eliminate poverty for those who were poor throughout their working lives. Nonetheless, the weighting would provide more adequate retirement benefits for such workers than would a strictly proportional formula.

Redistributive benefits were another aspect of the "insurance" against future economic slippage in retirement and a necessary part of the invention of retirement as a way of meeting the perceived needs of an industrial economy.

The committee also believed that benefits should be graduated so that low-wage earners and people who entered the system late in life would receive proportionately higher benefits. The committee believed that the goal of preventing dependency dictated that benefits be adjusted to meet "the relative needs of various classes of beneficiaries even though need is not a determinate in the individual case."\(^\text{320}\)

Managing the work force through inducement of voluntary retirement at age sixty-five required both advance assurance of minimally adequate retirement income and the opportunity to accumulate as much additional income as the worker's circumstances might allow in the form of private pensions, savings, and accumulated assets.

Under the Social Security benefit formula, while all workers had an equal opportunity to accumulate unlimited income for retirement, the weighting in the formula ensured a minimally adequate income level for those unfortunate enough never to raise

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319. See MARMOR ET AL., supra note 3, at 26-28, 31-34.
320. SCHIEBER, supra note 308, at 21.
their average earnings to a higher level. In fact, the CES report also recommended establishment of a voluntary additional pension program, aimed at “restricted groups in the population who do not customarily purchase annuities from commercial insurance companies,” as a way of providing lower- and moderate-income workers an opportunity to acquire additional retirement income rights to supplement the deliberately modest benefits under the contributory Social Security program.

The contribution formula, in contrast, remained static—all workers and their employers were to contribute a fixed percentage of earnings up to that wage level, regardless of the size of benefit any particular worker would ultimately receive. Thus, the financing of the system was based loosely on the group insurance model—a large pool of insured workers and their employers all contributing a fixed percentage of wages into the system to provide financing for all benefits. Neither employer nor employee

321. According to Robert Myers, one of the original consulting actuaries of the Social Security program, the wage replacement rates for single workers resulting from the original benefit formula ranged from 34% for maximum earners up to 73% for minimum earners. See id. at 23 (citing Robert J. Myers). This was prior to the 1939 amendments which added family benefits to the program. See id. In the final version of the Social Security Act of 1935 as in the current version of Social Security, the critical link between taxes paid into the system and benefits paid out was the taxable wage base. See id. at 21. The original wage base of $3000—$62,500 for 1996—established not only the maximum amount of wages subject to the tax but also the maximum earnings each year which would be credited to the worker’s account. Every qualified individual would receive, beginning on the date he or she attained age 65 or January 1, 1942, whichever occurred later, and ending at death, a benefit in equal monthly installments that was based on a two-tiered formula. See id. at 17. If total wages paid after 1936 were not more than $3000, the benefit would be half of 1% of total wages; if wages were more than $3000, the benefit would be paid at a monthly rate equal to sum of half of 1% of $3000 plus one-twelfth of 1% of the excess over $3000 up to $45,000, plus a twenty-fourth of 1% of excess over $45,000. Benefits could not exceed $85 a month. See The Social Security Act of 1935, reprinted in 50TH ANNIVERSARY EDITION OF THE COMMITTEE ON ECONOMIC SECURITY OF 1935 AND OTHER BASIC DOCUMENTS RELATING TO THE DEVELOPMENT OF THE SOCIAL SECURITY ACT 77-78 [hereinafter Social Security Act, CES 50TH].

322. See Report, CES 50TH, supra note 79, at 46.

323. The system was financed through taxes imposed on wages—employees were taxed at 1% of wages while every employer paid an “excise tax with respect to employees of 1% of wages.” See Social Security Act, CES 50TH, supra note 321, at 93. Wages were defined as remuneration for employment up to $3000 a year, and employment included any services performed by an employee except agricultural labor; domestic service; casual labor not in course of employer’s trade or business; labor performed by employees older than sixty-five; or labor performed by sailors, government employees, and nonprofit corporation employees. See id. at 93, 96.

324. See Report, CES 50TH, supra note 79, at 51-53.
contributions were directly linked to benefits ultimately payable to individual beneficiaries; FICA taxes were imposed as a financing mechanism for the system as a whole, not for individual annuities for each worker. Thus, while the contributory plan underwrote the earned-right entitlement, taxes paid by any one employer or employee bore only an indirect relationship to actual benefits paid.

c. The 1939 Act's expansions

One of the most extraordinary aspects of the 1935 Social Security Act was the inauguration of payroll tax contributions in 1937, five years in advance of the scheduled first payment of benefits and in the midst of a still extremely severe economic depression.325 Extensive controversy over the conservative character of Social Security's financing and benefit structure led to the formation of the first citizens' Advisory Council on Social Security, jointly appointed by Congress and the administration, and made up of policy experts and representatives from business and organized labor. The council was charged with examining several changes that would substantially expand the income redistribu-
tional aspects of Social Security.326

The 1939 report of the Advisory Council led to the 1939 Act, which did not change the essential Social Security entitlement but did greatly expand its redistributional effects. The Advisory Council's report reaffirmed the correctness of a contributory social insurance approach to old-age income maintenance and urged expansion of the approach to cover additional groups and problems.327 The report recommended broader protection than Con-

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325. Indeed, the inauguration of payroll taxes was blamed by some for a recession that began in June 1937. See ACHENBAUM, supra note 122, at 30.
326. See, Ball, CES 50TH, supra note 283, at 164-65.
Arthur Altmeyer [then chair of the Social Security Board] saw the forma-
tion of this council as an opportunity to move ahead with much more than financing changes. . . . The council was asked to consider whether it would be advisable to: begin monthly payments earlier, increase the amount of the monthly benefits payable in the early years, provide benefits for the disabled and survivors, and extend coverage to additional groups.

Id. at 165.

The council believes that [the contributory social insurance program's] method of encouragement of self-help and self-reliance in securing protection in old age is essentially in harmony with individual incentive within a democratic society. It is highly desirable in preserving American institu-
gress was willing to approve; nonetheless, in the 1939 Act the essential characteristics of the current Social Security family benefit were established. 328

The overall impact of the 1939 Act was to increase the redistributive impact of Social Security by providing dependents’ and survivors’ benefits in addition to workers’ benefits, while maintaining the basic earnings-relationship of the entitlement. 329 The 1939 Act also accelerated payment of the first benefits under the system to 1940, two years earlier than had been planned under the original legislation, and revised the financing schedule to put the system on a “pay as you go” rather than advance funding basis. 330 The Advisory Council, if not Congress, clearly anticipated that providing for an older worker and his or her spouse through the advance entitlement of Social Security would eliminate the need for broad antipoverty programs aimed at the elderly, even as the numbers of

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328. See Ball, CES 50th, supra note 283, at 166-67.

329. See id. at 166-67.

330. See id.
the elderly were expected to increase through the century.\footnote{See \textit{generally id.} at 165-67 (discussing the recommendations of the 1939 Advisory Council). In fact the Advisory Council's report anticipated growing numbers of elderly, estimating that by 1980, 14\% of the total population would be sixty-five or older, compared to 6.3\% in 1938—under current estimates, the 14.7\% probably will not be reached until about the year 2000. \textit{See} \textit{Schulz}, \textit{supra} note 190, at 266-68.}

d. \textit{universal coverage and private pensions}

Of particular importance to the coordination of Social Security with private pensions is the rejection in 1935 and later of suggestions that workers covered by a private pension should be excluded from Social Security. The original proposal was to cover all manual and nonmanual laborers earning less than $250 per month, with the exception of government and railroad employees who had fairly complete retirement plans already in place.\footnote{See \textit{Report}, CES 50TH, \textit{supra} note 79, at 49.} Private employer-provided pensions were not viewed as the equivalent of federal civil service or railroad pensions, and with good reason. Both of the latter systems had more or less government-guaranteed sources of financing, and workers with long service were virtually assured of receiving their pensions.\footnote{See \textit{Greenough} \& \textit{King}, \textit{supra} note 216, at 38-40, 58-59.} Private plans, on the other hand, were few in number, and many, if not most, had failed or gone bankrupt during the economic collapse earlier in the decade; private plans could not be considered any sort of alternative to a government-sponsored plan.\footnote{See \textit{Gordon, Business, Labor, and Politics}, \textit{supra} note 35, at 253-58; see also \textit{Orloff}, \textit{supra} note 100, at 277-79 (discussing the inadequacy of private pension plans in the 1920s and 1930s).}

Coverage of workers under the 1935 Act was more severely limited in category although the wages of workers in all categories of employment covered by the Act were included up to the $3000 contribution and benefit base. Several sets of workers were totally excluded: farm workers, domestic servants, self-employed workers, employees of nonprofit institutions, and others.\footnote{See Social Security Act, CES 50TH, \textit{supra} note 321, at 96.} At the time, Congress rejected recommendations by the 1939 Advisory Council to extend coverage to these groups for reasons that have been debated at length by historians.\footnote{See \textit{Orloff}, \textit{supra} note 100, at 292-93; \textit{Quadagno}, \textit{supra} note 100, at 107-12.} Nonetheless, coverage under Social Security was gradually expanded from 1935 through the 1983 Social Security Amendments, which covered the last large
groups—federal and nonprofit sector workers—so that well over 90% of the work force is now covered under the system. 337

Most important for understanding the relationship between Social Security and private pensions, the Roosevelt administration and the House of Representatives in conference on the 1935 Bill rejected a Senate amendment that would have exempted from Social Security coverage employees with private pension plans comparable to Social Security. 338 Throughout the development of Social Security prior to the 1935 Act, various groups pressed for a voluntary coverage approach similar to the private pension plans advocated by the "welfare capitalist" group, but were consistently rejected by the policy group drafting the legislation and by Roosevelt himself:

Roosevelt's officials did examine the experience of the welfare capitalist schemes, but they came to the conclusion that this experience demonstrated precisely that voluntary schemes were unworkable and that public, compulsory programs were essential. The committee's report on existing old age provision notes that "the half-century of experience with voluntary plans has shown that they have been inefficient and inadequate as sound social insurance measures." 339

The consistent emphasis on expanding coverage, and the aspirations for reaching universal coverage under Social Security, clearly indicate that private pensions were not seen by Social Security policymakers as either a partial or complete substitute for Social Security benefits for beneficiaries at any income level. Indeed, it seems likely that at this juncture private pensions were discounted as having any major role in the long-term task of providing for mass old-age retirement.

One question, therefore, is exactly how the benefits provided under Social Security were viewed in relation to benefits under the private pension system, which began its expansion roughly at the same time. If policymakers would not permit employers with pri-


338. See Myers, supra note 34, at 231.

339. Orloff, supra note 100, at 292 (citation omitted).
vate pensions to deprive their employees of Social Security coverage, why, in the 1942 Revenue Act, which established the first tax statutes requiring "nondiscriminatory" private pension plans, did Congress allow employers to eliminate pension coverage for their workers covered by Social Security?

V. TAX POLICY AND ENTITLEMENT: INTEGRATION AND NONDISCRIMINATION

By the beginning of World War II, the United States had in place a public social insurance system that had the potential, because of the redistributive elements of its formula, to replace needs-based public assistance in old age for anyone with a substantial work history—that is, the population that appeared to most Americans to be worthy of a nonstigmatized entitlement. The private employer-provided pension system was concurrently poised for a new development, with the strength of organized labor behind its postwar expansion, into a substantial source of income for better-off and well-organized industrial workers. The two systems expanded simultaneously but with little coordination, except in the integration provisions.

The weighting of the Social Security benefit formula in favor of low-wage workers, in the context of a program covering all workers but not all wages, created an entitlement program combining the elements of redistribution and earnings-based entitlement. The result was a prospective antipoverty program designed to ward off poverty in old age through benefits based on the relationship between working income and retirement income. Employers sponsoring private pensions had no such redistributional ambitions, yet the tax rules that developed from 1942 through 1986 effectively required a degree of redistribution through the nondiscrimination rules, which required some coverage of low-wage workers as the price for favorable tax treatment of amounts paid into pension trusts.\(^{340}\)

Why, then, was integration with Social Security allowed as an exception to nondiscrimination? The answer lies in underlying assumptions about the function of Social Security—assumptions shared by employers and the IRS and bolstered by the

"contributory" financing structure of the program, which conveyed the impression that benefits were related to contributions, rather than to earnings. Social Security was viewed as a substitute for private pension income by those "welfare capitalists" of the 1930s who supported Social Security only if it would relieve them of pension burdens. From their perspective, Social Security was a pension program for the low-paid, for which employers provided half the financing, through their FICA payments, like any other employee compensation cost.

Of course, the expansion of benefits and coverage under the program shaped Social Security into far more than a pension of last resort for low-wage workers. Social Security provided a federal, mandatory, and public redistributional income base that made broad, voluntary middle-class retirement possible. However, this base was deliberately limited in scope, providing at most a replacement for 40-50% of pre-retirement earnings and placing responsibility for the remaining 30-40% of necessary replacement of earnings on employers and individuals. The opportunity to add to Social Security benefits characteristic of an opportunity-based, rather than income-targeted, benefit structure, is at the heart of the "earned right" concept.

Private resources, including employer-provided pensions, individual savings, and investments, were apparently expected to provide part of the opportunity to accumulate retirement income for most adults who were part of the working population—or were dependent on someone who had been—for most of their lives. Means-tested poverty programs would provide subsistence for those—expected to be very few—who were not primarily or sec-

342. One indication of the importance of Social Security in underwriting mass retirement is the proportion of total income in retirement consisting of Social Security benefits. In 1992 elderly married couples age 65 and older received about 22% of their total income from private pensions, 12.8% from earnings, 40.7% from Social Security, and 22% from interest and dividends. See U.S. House of Representatives Comm. on Ways and Means, Where Your Money Goes: The 1994-1995 Green Book 864 (Brassey's ed. 1994). For poor couples, the percentage from pensions was 4.8%; for nonpoor couples, the percentage was 22.2%. See id. These figures probably overstate the role of private pensions, since most are not indexed to inflation, whereas Social Security benefits are increased every year under a cost-of-living increase provision. Thus, as recipients age, the real dollar value of the pension decreases while Social Security stays constant, thus becoming a larger percentage of total income.
343. See discussion supra Part IV.C.2.
ondarily attached to the full-time work force. One would expect that the income tax treatment of private pensions would be consistent with such a policy, whether by actively encouraging employers to establish pension supplements to Social Security or at least not discouraging provision of pensions to workers at all earnings levels.

The inception of the income tax followed establishment of the first private pensions and substantial use of annuities by several decades, and tax treatment of pension payments and trusts posed special problems for writers and administrators of the Internal Revenue Code from the beginning. Because private pensions represent a voluntary deferral of income that might otherwise be paid to the individual worker, the proper timing of taxation of the amounts deferred, as well of as any earnings that might accrue on those amounts, had to be determined. Favorable tax treatment of private pensions—that is, deferral of taxation for employees combined with a current deduction for employers who contribute to pension plans—developed into an elaborate incentive system and a key tool for federal government encouragement of private pensions.

In effect, the Code uses a carrot-and-stick approach to encourage employers to set up pension plans for their work forces—the carrot is the tax benefit of establishing a qualified pension plan and the stick is the limit on that benefit imposed by the nondiscrimination rules that require some provision of benefits for low-wage workers as well as high-wage workers. The integration rules represent the escape hatch out of the nondiscrimination rules for employers who want to provide higher benefits to high-wage workers. In an integrated plan, low-wage workers will earn lower benefits than they would in a nonintegrated plan, while high-wage workers will be allowed a higher level of benefits than the nondiscrimination rules generally permit in a nonintegrated plan.

The nondiscrimination rules governing the tax treatment of

344. See HABER & GRATTON, SEARCH FOR SECURITY, supra note 100, at 108-10. An old-age insurance program is not only an improvement upon the method of [poor] relief, but is also aimed to control and reduce the inevitable pressure to divert a larger and larger proportion of public funds in the form of free pensions to aged persons. The value to society of preventing dependency in old age, as far as possible, must be weighed against the cost of the insurance method.

S. REP. No. 76-4, at 12 (1938).

345. See discussion supra Part III.

private pensions were enacted as part of the Revenue Act of 1942, following enactment of both major Social Security Acts by several years.347 The role of Social Security in conjunction with private pensions, as part of a system providing for retirement income security, may have been tangentially considered in the development of that legislation, but it is clear that neither the redistributive elements in the Social Security benefit formula nor the role of redistribution in making middle-class retirement possible were a focus for legislators in 1942.

In fact, while the principles underlying the nondiscrimination rules mirror the benefit structure under Social Security—benefit amounts reflect wages earned in a roughly proportional structure insuring only coverage, not minimum benefit levels348—integration can be viewed as reflecting a static, almost class-based approach to retirement income. Pension integration was based on the assumption that Social Security was sufficient for low-wage workers who were presumed not to need a supplement, while private pensions to supplement Social Security were codified as a right only for high-wage workers. In effect, integration grafted a targeted, means-tested approach onto the earnings-based entitlements of Social Security and private pensions, vitiating the essential promise of opportunity to accumulate without imposition of income tests in retirement that is embedded in both the public and private entitlements.

While the integration rules can be seen as logical from a certain perspective, they were not a natural or inescapable part of the pension regulatory scheme codified in 1942. Rather, they were the product of a flawed understanding of the function of Social Security in conjunction with private pensions and were based on a conception of worker welfare that bifurcated the world into low-wage Social Security recipients and high-wage private pension recipients.

A. Tax Treatment of Private Pensions Prior to the 1942 Revenue Act

Employer-provided pensions in the pre-income tax era generally were paid out of current operating revenues of the em-

348. See id.
ployer, along with other employee-related obligations. As discussed in Part IV, since such pensions were generally considered gratuities rather than enforceable obligations, there was scant incentive for any advance financing of future pension payments. In the event an employer wished to fund pension promises, well-established common law principles of trusts provided a basis for setting up trusts of which employees might be the beneficiary. In the absence of personal or corporate income tax, the main legal considerations for employers involved common law contract concerns about enforceability of the pension promise itself. 349

Once the corporate and individual income tax was in place—from 1913 on—tax considerations began to play a more important role in employer decisions to establish pension plans. The Treasury Department decided early on that actual pension payments to retired employees should be deductible as ordinary and necessary business expenses and soon afterward allowed deductions for contributions to pension trusts so long as the trust was organized as an entity separate and distinct from the corporation. 350

The first statutory provision for tax treatment of employer-sponsored pension plans came in the 1921 Revenue Act, 351 which provided tax-exempt treatment for contributions to and earnings of stock bonus or profit-sharing trusts established by an employer “for the exclusive benefit of some or all of his employees.” 352 This provision was later amended in the 1926 Revenue Act 353 to include “pension plan” trusts that were not stock plans. 354 The legislative histories of the 1921 and 1926 provisions reveal little discussion of retirement income planning for employees; the focus appears to have been primarily, if not solely, on identification of the proper taxpayer and proper timing for taxation of contributions to and payments out of employer stock and profit-sharing plans. 355

349. See discussion supra Part IV.
350. A 1914 Treasury Department ruling allowed deductions for pensions as paid to employees. See T.D. 2090, 16 Treas. Dec. Int. Rev. 259, 281 (1914). A 1919 ruling held that employer contributions to a pension fund were deductible provided the fund was a separate and distinct entity. See O.D. 2-19-165, 1 C.B. 224 (1919).
352. Id.
354. See id.
355. For a discussion of this issue between Senators Reed and Smoot, see 61 Cong. Rec. 7113 (1921), and excerpts from Senate Finance Committee and Confer-
By the late 1920s, therefore, just as employers were shying away from setting up new pension plans because of the cost of carrying through on the retirement promise, the basic elements for tax treatment of private pensions was in place: immediate deductions for employers making contributions to pension trusts, in which earnings on contributions would accumulate without tax, resulting in no taxable income to the participating employee until payment of benefits in retirement. There were clear and obvious tax advantages in establishing trusts that might have little to do with actually funding employee retirement income promises, particularly since the relevant Code provisions used the term “distributees” rather than employees to identify those benefiting from the trust and allowed revocable as well as irrevocable trusts.


Until 1942 no legislative restrictions existed to limit employers’ interpretation of the Code language requiring that pension plan trusts be for exclusive benefit of “some or all employees.” The apparent result was that some plan sponsors established plans heavily favoring highly paid employees and shareholders as insurance companies began marketing plans based on the tax advantages. While the Treasury Department began challenging these trusts in the late 1930s for violating the requirement that plans be for the “exclusive benefit” of employees, no real limits were placed on amounts contributed to plans favoring highly paid employees until the Revenue Act of 1942.

It has been argued that the nondiscrimination rules of the 1942 Revenue Act were intended to raise revenue by limiting taxpayer abuse of the tax deferral available to employers establishing pension plans but not to ensure worker income security in retirement. “Abuse” in this context is the ability of taxpayers “to take

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356. See McGill, supra note 221, at 23; Munnell, supra note 46, at 31-32.
357. See Seidman, supra note 355, at 850-51.
358. See Altman, supra note 86, at 451.
359. See id. at 450-51.
361. See Altman, supra note 86, at 439-42.
unintended advantage of imprecise statutory language in order to reduce their tax liabilities.\textsuperscript{362} In the case of pensions, the imprecise language in question included “exclusive benefit” and “some or all employees,” phrases that gave considerable latitude to employers in determining which employees would be credited with benefit rights under a pension plan.

This analysis holds that the statutory language that addressed the problem by preventing “discrimination in favor of highly paid employees” should be viewed as anachronistic in focusing on the problem of highly paid employees taking advantage of the Code, rather than on insuring adequate retirement income for most employees.\textsuperscript{363}

[In making proposals in 1937 to make pension trusts irrevocable and require coverage of more than a few “key men,”] \textsuperscript{364} rather than seeking either to eliminate the subsidy or to marshall the natural motivation of taxpayers to reduce their taxes, the Treasury instead seemed to be focused on differentiating the taxpayers concerned with tax reduction from those genuinely concerned with retirement planning. In other words, the focus was on taxpayer abuse, not worker security. Consistent with this perspective, the Treasury statement concluded: “\textsuperscript{364}It will require very careful study to correct the \textsuperscript{some-or-all language} in such a way as to prevent abuse by the guilty without doing injury to the innocent.”

The key question is what legislators and employers in 1942 would have defined as “worker security” and “taxpayer abuse.” In light of the evolution of the concept of entitlement in the retirement income context in the years preceding this legislation, “worker security” in a private pension or Social Security entitlement context was just as likely to mean retirement income benefits at levels proportionate to pre-retirement income, rather than at a

\textsuperscript{362} Id. at 439.

\textsuperscript{363} See id. at 440-42.

\textsuperscript{364} Id. at 452 (footnote omitted).

In a written statement [presenting the 1937 proposals to Congress], the Deputy Commissioner of Internal Revenue explained “that some taxpayers are attempting to convert into a tax-avoidance mechanism a statutory provision designed to encourage pensions” and linked the abuse to the “some or all” language. \textit{This abuse of the plan for tax avoidance or reduction we wish to prevent.}

\textit{Id.} at 451-52 (footnotes omitted).
level satisfying an outwardly imposed income maintenance target. Thus, the nondiscrimination rules can be seen as quite consistent with the historical precedents of the Social Security system—while the Treasury and employers could not agree on requirements for minimum vesting and maximum benefits, they could settle on nondiscrimination rules that were based on the principle of paying retirement benefits commensurate with the worker’s earnings during the working lifetime.

Employer opposition to Treasury proposals that would have required full vesting in benefits and payment of minimum benefits, and employer acceptance of the nondiscrimination approach as a substitute, have been cited as evidence that the target of the 1942 legislation was tax avoidance rather than worker security. However, if employers were willing to maintain truly irrevocable pension trusts that were required to provide benefits to more than just the highly paid owners and executives, which was the aim of the nondiscrimination proposals, worker security would clearly have been improved. It can therefore also be argued that the nondiscrimination approach was accepted precisely because of concerns about worker security even though it would likely be less effective in eliminating taxpayer abuse.

While taxpayer abuse was undeniably a strong concern of the drafters of the original nondiscrimination rules, an examination of administration and public testimony, and of questions asked by members of Congress during hearings on the Revenue Act of 1942 reveal equal emphasis on the need to encourage establishment of private pension plans to provide retirement income to workers.

First, the administration’s stated purpose in suggesting the nondiscrimination principle as a qualification requirement for pri-

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365. See id. at 453-55.

The two proposals [vesting and maximum benefit limits] were met with vociferous opposition from the business community which argued that the proposals were unrelated to tax avoidance. A partner in a leading pension management firm, for example, testified:

Treasury’s suggestions with respect to pension plans and trusts are advanced at this time in order to prevent the use of such trusts as tax avoidance devices. This of course, is a desirable objective. . . . [However,] . . . some of the standards suggested by [the Special Tax Adviser to the Secretary of the Treasury] have no necessary connection with tax avoidance. Such standards were obviously conceived to further certain undisclosed social objectives.

Congress failed to pass even a modified vesting proposal suggested by the Treasury or the maximum limitation on benefits.

Id. at 453 (footnotes omitted).
vate pension trusts desiring to receive the tax deferral treatment already in place in the Code was to make sure that the underlying purpose of the “tax subsidy” was carried out. Randolph Paul’s testimony before the House Ways and Means Committee in 1942 foreshadowed the rationale and result of what Stanley Surrey later defined as “tax expenditures,” in suggesting that the tax deferral available to pension trusts was a subsidy in the form of reduced or no taxation for specific taxpayer behavior—providing pension coverage—that is encouraged for essentially nontax purposes. Moreover, in response to congressional questioning about the administration’s purpose in proposing not only nondiscrimination, but extensive vesting for shorter-service workers and a limitation of $7500 a year on pensions paid from an exempt trust, Paul made clear that all of the administration’s proposals were designed to increase pension protection for lower paid workers:

The next point we made was that there should be reasonable employee coverage. . . . That requirement has to do with the fairness of the plan and it also has a great deal to do with tax avoidance, because it prevents the plan from getting the subsidy status unless a reasonable number of employees are covered; the purpose is to prevent the subsidy from being used only in behalf of the higher

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367. Randolph Paul stated:

The present treatment of pension trusts affords a tax subsidy to those trusts which meet the requirements set forth in the statute. This subsidy is at the expense of the general body of taxpayers. It was granted because of the desire to improve the welfare of employees by encouraging the establishment of pension trusts for their benefit. Our purpose in presenting our suggestions was to carry out this objective of the Congress by suggesting various provisions which would both make the present statute more effective in promoting the welfare of employees through such trusts and at the same time prevent utilization of such trusts for tax-avoidance purposes.

Thus, we suggested that only those trusts which are designed to benefit large numbers of employees should be permitted this favored treatment. . . . We have [also] suggested that the benefits must be extended in a nondiscriminatory fashion, so that the higher salaried employees in the trust cannot be favored at the expense of the lower salaried employees. . . . These suggestions at the same time would operate to safeguard the pension provision against its use as a tax-avoidance device.

Revenue Revision of 1942: Hearings on H.R. 7378 Before the House Comm. on Ways and Means, 77th Cong. 2405-06 (1942) (statement of Randolph Paul, special tax advisor to the Secretary of the Treasury) [hereinafter Revenue Revision of 1942].
salaried, key employees.

The next point has to do with the nondiscriminatory provision; it is somewhat like the requirement in the [preceeding] point. The mere fact that 70 percent of the employees are covered does not necessarily mean that the plan is equitable. For example, low-salaried employees might have a very nominal interest while the high-salaried officials received the major benefit under the plan.\footnote{368. \textit{Id.} at 2407.} The thrust of Paul’s testimony is to make the case that these proposals do address tax abuse, a reason for legislation that was acceptable to Congress; as well as providing additional coverage and benefits for employees. The very definition of tax abuse in the administration’s terms is a pension plan that receives a subsidy without providing for lower-wage workers. Worker security and prevention of tax abuse were merged as goals.

In ensuing questioning, and in most of the testimony of employers opposed to the Treasury’s proposals, the nondiscrimination provisions received less attention than the vesting, the $7500 limit and the requirement for coverage of 70% of all employees, excluding what Paul terms “casual employees,”\footnote{369. \textit{Id.}} which were strongly opposed by employers, and seemed to at least one witness to represent “social security” legislation rather than tax abuse prevention.\footnote{370. \textit{See id.} at 2482-83. See also the statement of Arthur Hansen, a consulting actuary: \textbf{Mr. Disney has made the remark in which he said that the committee at this session was not going to consider any amendments to the Social Security Act. You have dispensed with discussion of the Social Security Act, and I think right along with that, since these proposals of Mr. Paul are of a social-security nature, they should be deferred along with social-security, except as it is necessary to take care of the specific problems now existing.} \textit{Id.} at 2484. For employer reactions to the vesting and other proposals, see generally \textit{id.} at 2411-71 (statements by several companies).} In fact, the Committee scheduled this day specifically to hear public testimony and administration “clarifications” of its pension proposals because of employer, and some organized employee, outcries over the possibility that pension plans would have to be terminated because they could not meet the administration’s new requirements.\footnote{371. \textit{See id.} at 2405 (opening remarks of Chairman Doughton).}

Nonetheless, the nondiscrimination rules were also attacked by employers and other witnesses as having nothing to do with
prevention of tax abuse.

This [nondiscrimination requirement] seems to be a re-

statement of [the requirement to cover a reasonable clas-
sification not favoring highly paid employees]. . . . dis-

crimination can be differentiated from justifiable increased rewards for greater service but it would be most difficult to draft a sound retirement trust for which an employer could adopt with any assurance that it would meet this requirement.

The suggestions as to maximum pensions and other benefits would seem to rule out any intent to require identical treatment of all employees. But if this proposal does not prohibit trusts which will pay larger benefits to more highly paid employees, what is its purpose? What discrimination of importance can there be if payment of greater benefits be not discrimination?

I am also puzzled as to what possible relation this proposal has to tax avoidance. Certainly a trust does not be-
come a part of a tax avoidance scheme because its crea-
tors believe in providing greater rewards to its executive staff than to the rank and file of workers. 372

In fact, one witness went so far as to declare, “If Mr. Paul’s rec-

ommendations are designed to eliminate tax avoidance, it is my opinion that only [a proposal on timing of deductions] is neces-
sary.” 373

Finally, the congressional reports accompanying the legislation echoed the administration’s previous emphasis on providing benefits to lower-paid workers.

While this legislation was tax oriented rather than reform oriented, the need for the legislation, according to the re-

port on the 1942 bill by the House Ways and Means Committee, was that the provisions of the tax code which were intended to encourage the setting up of retirement plans were being considerably abused by the use of dis-

criminatory plans which either covered only a small per-

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372. Id. at 2468 (statement of Richard D. Sturtevant, Assistant Secretary, Jewel Tea Co.) (emphasis added). For other examples of statements in opposition to the nondiscrimination provision specifically, see id. at 2478 (statement of Arthur Hansen).

373. Id. at 2489 (statement of Nathaniel H. Seefurth, Compensation Research Bu-

reau).
centage of the employees, or else favored the higher paid or stockholding employees. It was contended that under the law then in effect, the officers of a corporation could set up pension plans for themselves without making any provision for other employees.

In reporting out the revenue bill of 1942, the House Ways and Means Committee stated that the amendments made to the bill (H.R. 7378) by the Committee were intended to remedy the two most serious abuses of the pension trust provisions—(1) limited coverage, and (2) discrimination in favor of higher-paid employees.374

The 1942 legislation proposed to address these problems by requiring pension plans to cover a minimum number of employees and to provide roughly similar benefits to low- and high-paid employees. The Ways and Means Committee report stated:

"Even such extended coverage would not by itself guarantee that the pension plan would be operated for the welfare of the employees generally, because the scale of benefits could be manipulated. Therefore, the scale of benefits must be nondiscriminatory. High-salaried employees should not be favored at the expense of the low-paid employees.

. . . . Determination of benefits according to a fixed percentage of wages should not be considered discriminatory even though it results in larger benefits to highly paid employees. However, the use of one scale for officials and a less generous scale for other employees would be discriminatory. . . . For a plan to qualify . . . the scale of contributions and benefits must be nondiscriminatory, with the exception that larger employer contributions and benefits may be provided for the lower paid employees. Contributions or benefits based upon the application of a fixed rate to compensation paid directly to employees are not intended to be considered in violation of this provision."375

374. SUBCOMM. ON FISCAL POLICY OF THE JOINT ECONOMIC COMM., 93D CONG., INTEGRATION OF PRIVATE PENSION PLANS WITH SOCIAL SECURITY, STUDIES IN PUBLIC WELFARE, PAPER NO. 18, 173, 191 (Comm. Print 1974) (prepared by Raymond Schmitt) [hereinafter PAPER NO. 18].

375. Id. (quoting the House Ways and Means Committee report for the Revenue Act of 1942) (emphasis added).
Putting aside whatever the parties may have thought their purpose was, some nonetheless view the very structure of the nondiscrimination rules as evidence that limits on taxpayer abuse were the underlying purpose of the legislation because much lower benefits could still be provided to low-income workers so long as they were proportionate to earnings. However, it can also be argued that the nondiscrimination rules reflect much the same philosophy as the Social Security benefit formula—that is, workers’ income in retirement should reflect their wage levels during their working lifetime, not their income status once they cease to work. It is quite likely that without Social Security, strictly proportional benefits would be insufficient to provide adequate retirement income for low-wage workers. However, earnings-based entitlements are by definition designed to give workers benefits according to work histories, not need at the time of retirement.

Business opposition to Treasury Department proposals for vesting and irrevocability of trusts in 1937 and 1942 reveals the continuing distaste of employers for undertaking pension obligations that must be fulfilled, based on the disastrous history of “welfare capitalism” in the 1920s and 1930s. Therefore, nondiscrimination rules that required coverage of low-wage as well as high-wage workers were clearly preferable to iron-clad requirements to actually pay retirement benefits. Such a preference need not have any connection to the relative efficacy of the nondiscrimination regime in limiting “taxpayer abuse” rather than insuring income security. In the absence of minimum vesting requirements, coverage and benefit requirements could be easily accommodated as part of a highly voluntary private pension sys-

376. See Altman, supra note 86, at 475-76. As Altman indicates, “[f]rom a taxpayer abuse perspective, this rule is sound.” Id. at 476. “It is important to note that proportions that are uniform in relation to salaries nevertheless may, in small plans, result in the allocation of the bulk of the employer contributions to the high paid employees.” Id. at 476 n.168.

Providing all employees with benefits or contributions that are uniform proportions of their compensation is not an act of favoritism towards the prohibited group. Rather, the deferred compensation is an extension of, and is consistent with, the employer's overall pattern of compensation. From a worker security perspective, however, the proportionate rule would be troubling, if it were not for Social Security. Lower income workers generally need a higher percentage of their final salaries than higher paid workers to be able to retire without sacrificing their current standards of living. Moreover, higher salaried people have a greater ability to save for retirement.

Id. at 476 (footnotes omitted).

377. See id. at 453.
tem that had never been designed to underwrite mass retirement on the scale that would develop after World War II.

In summary, the essential elements of nondiscrimination rules can be explained as well by concern for provision of pension benefits for low-paid workers as by concerns about taxpayer abuse. A regulatory structure allowing most of the tax subsidy to continue to flow to high-paid workers at the price of providing some benefits to low-paid workers hardly seems solely focused on limiting abuse of the tax system.

C. 1942 Revenue Act: The Role of Integration in the Nondiscrimination Framework

Even though the 1942 Act did not use the term "integration" specifically, the concept was an original part of the nondiscrimination rules. The main thrust of the nondiscrimination rules was to prevent discrimination in favor of corporate officers, stockholders, or highly compensated employees with respect to coverage, contributions, and benefits. However, the 1942 Act included what later became § 401(a)(5) of the Internal Revenue Code of 1954, which, notwithstanding the basic nondiscrimination requirements, stated that no plan would be considered to be "discriminatory ... merely because (a) it excludes employees the whole of whose remuneration consists of taxable wages under Social Security [or] (b) the contributions or benefits based on . . . remuneration . . . excluded from the Social Security tax base differ from contributions or benefits within this base."

In light of the concerns underlying the establishment of a compulsory and contributory system under Social Security—in particular the explicit refusal to allow workers covered by private pensions to elect out of Social Security—the 1942 Revenue Act integration provision seems to be an anomaly, a kind of reverse voluntary coverage under which employers were allowed to elect *not* to cover under a pension plan employees whose wages were completely covered by Social Security.

At the time of the 1942 Act, beneficiaries who had paid vir-

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tually nothing into the Social Security system were already receiving benefits, a result of the 1939 revisions intended to address widespread poverty among the elderly whose savings and pensions had been wiped out by the Depression. The advance-funding feature of Social Security was abandoned in the 1939 revisions in favor of "pay as you go" financing so that the link between workers' benefits and their tax payments into the system was minimal in actuarial as well as statutory terms.

Thus, it is not surprising that employers, and the IRS in consultation with them, would view Social Security as paid for by the employer and maintain that the employer should not, as a result, have to duplicate its coverage through a private-pension benefit. Indeed, employers apparently took for granted that no one would expect them to provide pension coverage for workers making $3000 or less, the maximum wages covered by Social Security. Most of the plans described to members of the Ways and Means Committee during the hearings on the 1942 Revenue Act provided either no or lower pension contributions based on earnings below $3000.

The reasoning of employers was probably typified by the testimony of Robert Gordon of National Dairy Products, describing how the company came to set up its contributory pension plan in 1941:

The first thing that came to our attention was that only 1,200 of our total number of employees [37,500] received over $3,000. Among those 1,200 were practically every employee that had a real influence on how the company went ahead, how it achieved success over its competitors. We also knew that the social-security-tax program was coming along and was going to do a job.

We pay a considerable amount of money in social-security taxes and all of our employees pay the same amount on their pay.

380. See discussion supra Part IV.
381. See discussion supra Part IV.
382. See, e.g., Revenue Revision of 1942, supra note 367, at 2414 ("To reflect social-security taxes and benefits, both contributions and pensions are correspondingly lower on the first $3,000 of salary than on portions of salary above this figure.") (statement of James L. O'Neill, Vice President, Guaranty Trust Co.). O'Neill explained that "[o]ur plan is designed to supplement the Social Security Act. On the first $3,000 of all salaries less is paid into the pension fund. On the first $3,000 we provide only 1-percent benefits." Id. at 2416.
So we decided this . . . we will have nothing paid into the plan by either employer or employee on salaries below $3,000, and we will let the social-security-tax program take care of the salaries under $3,000.

. . .

. . .[W]e think we can achieve retirements under this plan with the company paying only a part, and the employees, by forced savings . . . paying their part, and for all people under $3,000, we think that with the aid of the Social Security Act we have no real problem on retirements, and no real hardship. 383

At least two members of the Committee, however, saw inequity in this plan, if not hardship. Congressman Knutson led the following exchange:

MR. KNUTSON. If I understand your plan correctly, you folks have set out a saucer of cream . . . for the higher-ups and the rest get skimmed milk.

MR. GORDON. It is very thin cream.

. . .

MR. KNUTSON. And you do not do anything for those who get less than $3,000 a year. You leave them to the tender mercies of the Social Security Act.

MR. GORDON. We pay our full tax, in accordance with their pay, and they pay their full share.

. . .

MR. KNUTSON. I do not think much of your plan, because as to the people in the lower brackets who really need it, they have no opportunity to lay anything aside for old age, and they get nothing from your plan. Those people who get above $3,000 certainly ought to be able to lay something aside.

MR. GORDON. The people above $3,000 have tax burdens. They live, as you know, in accordance with what they make, and they do not save money. Maybe they should save money, but they do not save money.

. . .

MR. KNUTSON. You can pay your president $150,000,

383. Id. at 2427-29 (statement of Robert S. Gordon, general counsel, National Dairy Products Corp.).
but you cannot take care of those below $3,000 in your pension plan. It looks lopsided to me. I do not think much of your plan. And I think this is one of the things that the Treasury is aiming at.\textsuperscript{384}

The chairman of the Committee was even more blunt in his assessment of the lack of benefits for workers covered by Social Security in National Dairy Products' plan. The exchange between Chairman Doughton and Mr. Gordon is worth reproducing here at length, as it almost perfectly summarizes employer reasons for providing pensions as well as the problems with pension integration even today:

\begin{quote}
\textbf{THE CHAIRMAN.} How many employees are there in your company?

\textbf{MR. GORDON.} 37,500.

\textbf{THE CHAIRMAN.} How many are eligible for benefits under your system?

\textbf{MR. GORDON.} Two thousand get above $3,000.

\textbf{THE CHAIRMAN.} They are the ones that need it less; they are the highest-paid employees. On the basis of need, they are the ones that need it least; is that not so? . . .

\textbf{MR. GORDON.} I would say that a pension plan is not a charity. . . . We are not trying to give this money out on the basis of need. We are trying to provide for orderly retirement of people, and we say that with the aid of the social-security payments we can retire at 65 men who have gotten under $3,000 a year. Their needs are not large. They are willing to retire, and they do retire, and are happy.

\textbf{THE CHAIRMAN.} The social-security plan will take care of those in the lower brackets. Why would it not take care of all of them?

\textbf{MR. GORDON.} They have geared themselves up to a higher standard of living.

\textbf{THE CHAIRMAN.} These other people would maintain a higher standard of living, too, if they had more income. Now when they are old, you just want to turn them out to . . .
\end{quote}

\textsuperscript{384} Id. at 2428-28 (colloquy between Congressman Knutson and Mr. Robert Gordon, general counsel, National Dairy Products Corp.).
graze in an old field, having served all of their usefulness.

MR. GORDON. We are in a competitive society, and the men that have got the worth are supposed to earn what they are able.

. . .

THE CHAIRMAN. . . . It seems to me that you are giving to the ones that have plenty and to those that have nothing, you do not even give the opportunity of getting anything.

I never heard of such a thing.

MR. GORDON. In conclusion, I want to say that our whole plan was not intended to increase the cost to the corporation of retirements.

THE CHAIRMAN. I can see exactly what it was intended to do, but it is the worthiness of it that bothers me.

MR. GORDON. It accomplishes the end; it achieves retirement. Our people who have worked beyond the peak of their efficiency are retired, and we replace them with younger men. The older people are taken care of and do not become public charges. 385

Nonetheless, despite the concerns expressed in the preceding exchange, the nondiscrimination in the 1942 legislation allowed Social Security to provide total pension coverage for low-wage workers:

Thus, a plan in good faith designed to supplement the benefits under the Social Security Act . . . by making eligibility to the benefits of the plan dependent upon an employee receiving annual compensation in excess of $3,000 [the taxable wage base at that time], will not be considered by reason of that fact as based upon favoritism to highly compensated employees. 386

Legislators apparently saw no contradiction between integration and Social Security's aspirations of universal coverage. Instead, integration was presented as a logical necessity, certainly by employers, although the Treasury apparently did not publicly adopt this view. A later pension analyst summarized the result as

385. Id. at 2431 (colloquy between the Chairman and Mr. Robert Gordon, general counsel, National Dairy Products Corp.).

386. PAPER No. 18, supra note 374, at 191 (quoting a House Ways and Means report).
follows:

The basic idea of integration is simple. Social Security laws set a ceiling on the amount of wages subject to payroll tax. Since social security benefits are related to covered earnings, they also have a built-in ceiling. Thus, social security income replacement rates decrease as pre-retirement income increases. It was considered logical, therefore, to permit the private pension system to pick up where the social security system left off by providing supplemental benefits based upon earnings above the social security wage base.

Congress recognized this in 1942, when it first wrote into the law the proviso that although a tax-qualified plan could not discriminate in favor of the higher paid workers, its benefit structure could favor those with earnings above the social security ceiling provided that when the public and private benefits were considered together, their combined benefits did not give preference to the higher paid. So long as the ratio of combined benefits to earnings is no higher for employees whose wages exceed the taxable wage base than for those whose wages are fully taxed by social security, Congress said a plan would be held to be nondiscriminatory.\footnote{387. Id. at 175; see also Revenue Revision of 1942, supra note 367, at 2440-41, 2486-87 (discussing the nondiscriminatory provisions and the bases for determining discrimination).}

So, for example, assume that a worker whose earnings were less than $3000 per year—the wage base at the time—would receive Social Security benefits that would replace 40% of earnings. A worker earning $6000, twice the wage base, would receive a Social Security benefit replacing perhaps only 20% of total earnings. Under the integration principle, the low-wage worker could receive no private pension and the higher wage worker could receive a pension equal to 40% of earnings over $3000 without violating the principle of nondiscrimination since both workers would receive the same ratio of benefits to earnings—one from the public program and one from the private as well as the public.

The end result was a nondiscrimination scheme that attempted to ensure coverage of low-wage workers by tying tax benefits for high-wage workers to proportional benefits for low-
wage workers. Yet plans were allowed to essentially eliminate from coverage all employees with total wages below the Social Security wage base, on the grounds that such employees would be provided for under Social Security. This view—that private pensions can be truly "supplementary" to Social Security by giving benefits only to higher wage workers—logically follows from a "worker security" perspective as much as from the employer view that employers were already paying for the low-wage workers' pension through their FICA contributions.

By imposing a targeted total replacement rate on the combination of Social Security and the private pension—which is in essence how integration allows discriminatory benefit formulae to qualify as nondiscriminatory—the nondiscrimination rules can be said to have embodied one notion of worker security. Integration is reconciled with the nondiscrimination principle only by assuming that Social Security provides all benefits necessary for those under the wage base and that pensions are the legitimate way to increase replacement rates to a constant level for those above the wage base. Otherwise, Congress's allowance of integration makes no sense since integration, by definition, ensures that plan benefits will favor highly compensated employees over low-wage employees.

This conception of the retirement income system—a combination of two types of benefits coordinated to produce a combined target replacement rate for low- and high-wage workers—violates the entitlement principles of Social Security in two ways. First, inherent in the imposition of target replacement rates on the combination of public and private entitlements is the "top-down" assessment of need in retirement—measured by "adequate" or "excess" replacement rate—that the evolution of retirement entitlements has consistently resisted. Second, the assumption of economic dynamism and mobility that underlies the "opportunity to accumulate" principle of retirement entitlements is replaced in the nondiscrimination rules including integration with an assumption of static economic position. Low-wage workers are assumed to remain low-wage workers throughout their careers with the higher replacement rate under Social Security necessitating setting limits on excess replacement of wages in retirement for low-wage workers.

388. See discussion supra Parts III-IV.
D. The First IRS Regulation of Integration: 1943-1979

After passage of the 1942 provisions, the Treasury Department began almost immediately to attempt to restrict employer use of integration to reduce or eliminate pension benefits for workers covered by Social Security. An examination of both initial and later Treasury guidance shows that the elaborate integration rules of later years were all derived from three factors: first, the Treasury’s initial effort to determine the portion of Social Security benefits attributable to employer contributions; second, assumptions made concerning the value of all Social Security benefits relative to the primary insurance amount (PIA), which is the basic Social Security benefit produced by applying the benefit formula to the worker’s lifetime earnings record; and finally, the amount of pre-retirement income replaced by Social Security for workers at the wage base.

The Treasury Department’s approach to the integration rules was based on the fundamentally flawed premise that Social Security benefits were tied to FICA tax payments. This premise led directly to a conclusion that individual workers’ benefits could be attributed to specific employer FICA tax contributions and, from there, to the presumption that employers could be “credited” with their payments for those benefits. The entire subsequent development of the integration structure was based on this mistaken understanding of the relationship between FICA tax payments and individual benefit amounts, which confuses the benefit and financing structures.

In Mimeograph 5539, issued by the IRS in July 1943, the basics of offset and excess integration formulas were established. In offset formulas, employers would be allowed to subtract 150% of PIA from a normal retirement benefit, on the grounds that 100% of Social Security benefits were attributable to employer contributions and that a worker and spouse received 150% of PIA as a benefit from Social Security. Excess plans would be allowed to pay no benefits based on earnings below the “integration level”—the wage base of $3000—and could pay up to 25% of

389. See generally Altman, supra note 86, at 450-54 (describing the Treasury Department’s motives behind integration rules in the Revenue Act of 1942).
390. See generally MUNNELL, supra note 46, at 32-35 (describing integration guidelines).
391. See Mime. 5539, 1943 C.B. 500 (explaining Treas. Reg. § 19.165(a)(3)-(1)).
392. See id.
earnings above the integration level.\textsuperscript{393} The 25% figure was to be increased by .25% each year after 1941.\textsuperscript{394} Twenty-five percent apparently "approximated the ratio of employer-sponsored Social Security benefits to average earnings for workers whose average earnings were equal to the taxable wage base."\textsuperscript{395}

In these calculations the IRS made several assumptions that underlie all subsequent modifications to the integration rules. First, the offset formula limits established in Mimeograph 5539 reveal the IRS's assumption that 100% of Social Security benefits were attributable to employer contributions even though integrated formulas allowed under the 1942 Act would affect many younger workers with decades of employment who would contribute substantial amounts to Social Security.\textsuperscript{396} While this attribution percentage would decline in succeeding years, the initial 100% baseline meant the IRS accepted the philosophical proposition that Social Security was in part a type of employer-provided pension that employers were entitled to setoff against their own benefit promises to employees.

Second, the offset percentage took dependent and survivor benefits into account, allowing employers to take credit for auxiliary Social Security benefits in reducing their private pension plan commitments even though their plans may not have provided similar benefits. Moreover, while Social Security family benefits were provided without any reduction in the initial benefit paid to the worker—a worker and spouse would receive 150% of the PIA—private plans typically reduced benefits paid to a retiree if benefits would be paid to the worker's surviving spouse under a joint and survivor annuity option.\textsuperscript{397} Even under the flawed premise upon which the IRS relied in developing these rules, employers were given a substantial advantage in being allowed to offset 150% of the basic Social Security benefit against a private benefit that would pay only the equivalent of 100% of PIA to a worker and spouse over their lifetimes.

Finally, by allowing employers to pay nothing in benefits below the wage base while paying benefits equal to 25% of earnings below

\textsuperscript{393} See id.
\textsuperscript{394} See id.
\textsuperscript{395} See SCHULZ & LEAVITT, supra note 14, at 21-22.
\textsuperscript{396} See Mim. 5539, 1943 C.B. 500.
above the wage base, the IRS was acting on the assumption that 25% represented the percentage of earnings at the wage base actually replaced by Social Security benefits in retirement. Since 100% of the benefit was already attributed to the employer, private pension plans could pay that much more in benefits to employees with earnings above the wage base. This 25% figure cast a long shadow, forming the basis for excess plan benefits, as modified over time, up until the 1986 Tax Reform Act, despite major revisions in the structure and calculation of Social Security benefits that made it almost irrelevant in replacement rate terms.

Beginning in 1951 the IRS issued regular amendments to the regulations in an attempt to adjust these initial percentages to take account of several major expansions in the Social Security program, beginning with increases in the taxable wage base and in the maximum PIA as a percentage of average earnings up to the wage base. The percentage of Social Security benefits—still including ancillary benefits—attributable to the employer was reduced, producing an increase in the 25% excess figure to 37.5%, and a reduction in the allowable offset to 140% in 1950. During a series of Social Security amendments that increased the PIA as a percentage of the wage base, the IRS steadily reduced the percentage of benefits attributable to employers, so that the excess percentage remained at 37.5%, up until 1967. At that point, as reflected in Revenue Ruling 61-75, the IRS attributed 78% of the value of the maximum Social Security benefit package to employer contributions; since Social Security was estimated to replace 47.625% of employee wages at the maximum level, the employer was considered to have "paid" for 37.145% of the benefit, which was rounded up to 37.5%.

The Treasury Department undertook a comprehensive examination of pension integration after the President's Committee on Corporate Pension Funds issued a report in 1965 that criticized...
the current integration percentages:

[The current integration formula attributes] to the employer more benefits than he has paid for with his own contributions, which in fact are equal to those of his employees. In fact, [the integration percentage] attributes to the employer all benefits that the employees have not paid for by their own contributions.

The Committee . . . recommends that qualified corporate plans be permitted to continue to integrate with OASDI but that, as to benefits earned after the date of the change, the employer be given credit for no more than one-half of the social security benefit. This would be consistent with the financing of OASDI benefits through equal tax contributions from employers and employees.405

The IRS's review resulted in a new estimate that would reduce the excess percentage down to 24%, based on the increase in the taxable wage base since 1961 from $4800 to $6600; after requesting and receiving public comment on possible reductions in the excess percentage, the IRS announced interim regulations temporarily allowing excess percentages up to 27.25% for defined benefit plans, 6.80% for defined contribution plans, and a new maximum offset of 85%.406 Two years later, after enactment of the Social Security Amendments of 1967,407 the IRS effectively accepted the earlier recommendations of the Presidential Committee408 and based its integration percentages on the assumption that 50% of Social Security benefits were attributable to employee contributions.409

In Revenue Ruling 69-4,410 the IRS set new integration limits: a 30% excess limit—employers could pay benefits that were 30% of wages above the wage base and zero below; and a 75% offset limit—employers could reduce private pension benefits by 75% of PIA.411 This bold move did not last long, however, as the Social

405. PRESIDENT'S COMMITTEE ON CORPORATE PENSION FUNDS AND OTHER PRIVATE RETIREMENT AND WELFARE PROGRAMS 63 (1965) [hereinafter PRESIDENT'S COMMITTEE].
408. See PRESIDENT'S COMMITTEE, supra note 405, at 62.
410. Id.
411. See id. at 119-21. While the actual calculations of the approach used in
Security Amendments of 1971\(^{412}\) provided a basis for the IRS to move the excess percentage back up to 37.5%, in Revenue Ruling 71-446.\(^{413}\) The IRS explained this change as a result of two changes in its methodology: first, it began considering for the first time disability benefits as an ancillary benefit, which increased the total Social Security benefit package from 150% of the PIA to 162% of the PIA; and second, the basic benefit calculation for the PIA was increased from 36% of the worker’s average monthly wage to 43%.\(^{414}\)

The basic outline of the integration rules set in Revenue Ruling 71-446\(^{415}\) did not change substantially for over ten years, and even then, the Tax Equity and Financial Responsibility Act of 1982 (TEFRA)\(^{416}\) changed the rules mainly for top-heavy plans although the limit for all defined contribution excess plans was reduced from 7% to 5.7%. Still, the mechanics of the integration rules were basically set in Revenue Ruling 71-446, and it remained the fundamental guideline for employers until after the 1986 Act changes.\(^{417}\)

The IRS’s approach to regulation of integration is emblematic of a technical response to a philosophical dilemma. Clearly integration inherently contradicted the purpose and spirit of the nondiscrimination rules by allowing employers to pay fewer or no benefits to low-paid workers than to high-paid workers. If one views the tax advantages flowing from tax qualification of plans under these rules as a general taxpayer subsidy for retirement savings, workers whose benefits were eliminated or substantially reduced by integration were subsidizing the higher-pension benefits paid to their employers and higher-paid colleagues.\(^{418}\) The nondiscrimination rules were developed in part to limit this perceived subsidy.

Revenue Ruling 69-4 yielded a 27% integration percentage, the ruling allowed employers to use a percentage as high as 30% in order to reduce the cost impact on employers. See id.


\(^{414}\) See id.

\(^{415}\) Id.


\(^{418}\) See Altman, supra note 86, at 481, 484.
The IRS was bound, however, by a mistaken assumption embedded in the statutory provision for integration—that Social Security benefits were part of the employer-employee relationship upon which private pensions were based; therefore, employers should be able to treat FICA tax payments as another type of funding vehicle for employee pensions. Regardless of limits placed on the amount of the offset, the integration rules inevitably resulted in reducing the role of higher-paid workers in financing redistribution under Social Security. Since employers could essentially reduce their overall pension obligations to lower-paid workers while maintaining the high level of benefits needed to attract and retain higher-paid workers, integration ultimately meant that low-paid workers shouldered a higher tax burden while receiving less in retirement income, precisely the opposite of the intended result of the Social Security benefit structure.

VI. REFORMING INTEGRATION

As the IRS attempted to delineate the limits of integration through rulings, various efforts to eliminate or reform integration were mounted in the legislative arena from at least 1953 through the 1986 Tax Reform Act. The remarkable resilience of the integration provisions, in the face of repeated attacks from pension advocates, Treasury officials, and members of Congress, is not solely due to the influence of employers whose benefit costs would undoubtedly be much higher without integration, although that influence probably played an important role. Integration at some level was assumed by both opponents and proponents to be a necessary element of coordinating Social Security and private pensions, and thus attempts at reform inevitably fell short.

The strength of employer opposition to changes in integration was fueled in part by the employers' view of their FICA tax payments as being the source of their employees' benefit entitlement. The IRS's technical response to the problem of implementing integration was to determine the "true" portion of benefit "paid for" by employers, based on the confusion of contributory financing with earnings-based benefit structure. Employers' own
views of their payments to Social Security reflect this same perspective, thus lending a consistent theoretical basis to the vociferous business antagonism to any attempts to eliminate integration.

Legislative proposals to reform integration, however, were also driven by impulses contrary to entitlement principles, inevitably leading to acceptance of the need for some integration. As discussed below, many analysts rejected, on essentially economic grounds, the argument that employers should get credit in their private pension plans for their FICA tax payments to the public plan. Nonetheless, most pension analysts and reformers were unable to advocate outright elimination of integration because of the possibility of low-wage workers receiving more in retirement income—from the combination of Social Security and nonintegrated private pensions—than they had earned while working.\(^\text{423}\)

As a result, reform proposals were based on mistaken assumptions and essentially misguided goals. Legislators and some reformers assumed that Social Security was interchangeable with employer-financed private pensions containing an identifiable "employer-provided" share. All parties to the debate agreed with the goal of adequate, but not "excessive," income replacement in retirement for workers at low-wage levels from the combination of Social Security and private pensions.\(^\text{424}\) Neither proposition is sustainable, however, in light of the entitlement principles upon which Social Security is based.

Nonetheless, policymakers were apparently unwilling to countenance the consistent application of entitlement principles if that resulted in low-income workers receiving more in benefits than they received in wages while working, even if such a subsidy was required to prevent recourse to poverty-based programs. The result was a series of legislative reform attempts that did not address the central contradiction between integration and entitlement.

A. Extent of the Integration "Problem"

The extreme complexity of the permissible integration methods under IRS rulings did not discourage employers from taking advantage of the opportunity these methods presented. While the

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\(^{423}\) See PAPER NO. 18, supra note 374, at 174; MUNNELL, supra note 46, at 55-59.

\(^{424}\) See generally Alicia H. Munnell, ERISA—The First Decade: Was the Legislation Consistent with Other National Goals?, 19 U. MICH. J.L. REFORM 51, 58-60 (1985).
data are not completely reliable for pre-ERISA years, integration was apparently a widespread practice in the years leading up to enactment of ERISA in 1974.\textsuperscript{425} A study conducted by the Congressional Research Service (CRS) after enactment of ERISA, using data collected prior to ERISA's effective date in 1974, estimated that about 60\% of all plans were integrated and that integration affected 25\% to 30\% of the 30 million participants in those plans.\textsuperscript{426}

The CRS study revealed distinct differences between treatment of workers in large plans covered by collective bargaining agreements, usually not integrated, as opposed to small company plans, which were more likely to be integrated, particularly plans covering salaried employees.\textsuperscript{427} Sixty-four percent of smaller plans covering twenty-five or fewer employees—accounting for about 10\% of all covered workers—were integrated, whereas only 29\% of large plans—covering 90\% of workers—were integrated.\textsuperscript{428} Most integrated plans were not complete offset plans—that is, they provided some benefits based on earnings below the integration level.\textsuperscript{429}

Many analysts argued that integration did not result in substantially lower benefits for most low-wage workers, particularly since pure offset plans, which would eliminate pension benefits altogether for some workers, were almost nonexistent.\textsuperscript{430} Thus, even though the practice of integration was widespread, its impact on individual workers could be viewed as not particularly severe since most employers refrained from the maximum permissible integration levels.

The data are not conclusive as to the effect of integration on individual workers in the wide variety of plans using integration; however, the law clearly allowed for very substantial reductions in low-wage worker pensions:

Under [pre-1986] law, low-wage and short-service workers sometimes received little or no benefit from an integrated pension plan. Firms could offset as much as 83-1/3

\begin{thebibliography}{9}
\bibitem{426} See \textit{PAPER No. 18, supra} note 374, at 174.
\bibitem{427} See \textit{id.} at 175.
\bibitem{428} See \textit{id.}
\bibitem{429} See \textit{id.}
\bibitem{430} See \textit{SCHULZ \& LEAVITT, supra} note 14, at 55-56.
\end{thebibliography}
percent of the social security benefit from the pension accrual. Since the replacement rate values of social security benefits are proportionately higher for lower-wage workers, offsetting a large percentage of the social security benefit against the pension accrual in some cases wiped out the entire pension. Simply stated, the social security offset was larger than the pension accrual. In still other cases, short-service workers had their entire pension accrual offset by their full-career social security benefit. This was true even at relatively high earnings levels.431

Analysts might well argue that if most employers did not use integration to reduce benefits to the maximum level allowed by the law, then limits that reduced that maximum level should not present any substantial additional costs for employers. The ferocity of employer opposition to changes in integration is indicative of a perhaps greater level of savings realized by the practice than can be surmised simply from the survey data.

B. Attempts to “Reform” Integration

The first attempt to eliminate or substantially amend integration in the statute came in 1954 when Congress undertook a complete revision and codification of the Internal Revenue Code.432 The House version of that legislation contained a provision that would have replaced the discretionary language in the statute with a bright-line rule allowing employers to simply disregard the first $4000 of employee compensation in benefits provided under a private plan.433 The Senate rejected this approach and suggested further study because of the impact on many plans.434 While criticism of integration continued, the next major reform effort did not occur until almost twenty years later.

The private pension promise remained almost as elusive in the postwar period as it had been in the early years of the century. Without requirements for funding and vesting of benefits, employers in noncollective bargaining situations had great freedom to de-
sign plans that would benefit few rank-and-file workers or those who left the employer before retirement age. The wholesale review of pension laws undertaken as part of the development of ERISA legislation in the early 1970s was motivated primarily by concern for the failure of employers to fulfill the pension promises made to employees.435

The perception among policymakers that integration was simply a way of depriving employees of promised pension benefits led to a concerted effort to eliminate integration as part of ERISA in 1974.436 A statement in the report of the House Ways and Means Committee describing the House version of ERISA’s provision on integration accurately summarized the dilemma of lawmakers attempting to ensure that workers received the full benefit of both Social Security and private pensions in the context of a voluntary employer-provided system:

On the one hand, the objective of the Congress in increasing social security benefits might be considered to be frustrated to the extent that individuals with low and moderate incomes have their private retirement benefits reduced as a result of the integration procedures. On the other hand, your committee is very much aware that many present plans are fully or partly integrated and that elimination of the integration procedures could substantially increase the cost of financing private plans. Employees, as a whole, might be injured rather than aided if such cost increases resulted in slowing down the rate of growth of private retirement plans.437

As a compromise, the House bill contained a provision to prohibit integrated pension plans from reducing the pension benefits already being paid based on increases in social security benefit levels.438 In the conference on ERISA, a substitute provision was

435. See Michael S. Gordon, Overview: Why Was ERISA Enacted?, in U.S. Senate Special Comm. on Aging, The Employee Retirement Income Security Act of 1974: The First Decade 6 (1984). In particular, the case of Studebaker workers who were denied pensions when the company ceased operations, despite decades of employment and coverage under the plan, provoked widespread public indignation and subsequent congressional reaction. See id. at 8.


438. See id.
agreed on, which would have frozen the integration level at its 1971 amount until June 30, 1976. This would have essentially forbidden plans to increase the integration level based on increases in Social Security benefits during that period although plans that had already increased their levels would not have been required to reduce them to the 1971 level.\footnote{439} Even though this provision was agreed upon in the conference report as approved by both houses, the outcry from employers created such pressure for repeal that in an unusual move, a concurrent resolution calling for further study of integration and deleting the section from the final version of the legislation was approved before it could take effect.\footnote{440}

The pressure for reform continued with the Carter administration’s 1978 proposal to overhaul the rules completely.\footnote{441} This proposal was based on the common criticism that the private pension system did not adequately provide for lower-paid workers, partly as a result of the reduction integration allowed in benefits for those workers and despite the tax subsidy provided to employers to induce such coverage.\footnote{442} The administration’s proposal attempted to ensure that low-wage workers would receive at least a minimal level of benefits by preventing a complete offset of the private pension benefit. The proposal also attempted to limit the replacement of earnings above the integration level to 2.1 times the percentage of earnings replaced below the integration level.\footnote{443}

The effects of the administration’s proposal for excess and for offset plans are demonstrated in the following tables:\footnote{444}
BENEFITS AS A PERCENTAGE OF EARNINGS AT RETIREMENT UNDER PRE-1986 LAW AND UNDER THE 1978 PROPOSAL

<table>
<thead>
<tr>
<th>Statute/Proposal</th>
<th>Final Average Pay</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Excess Plan</strong></td>
<td><strong>$5000 $15,000 $30,000 $50,000 $75,000 $100,000</strong></td>
</tr>
<tr>
<td><strong>PRE-1986 LAW</strong></td>
<td></td>
</tr>
<tr>
<td>Pension only</td>
<td>0% 10% 23% 28% 31% 32%</td>
</tr>
<tr>
<td>Pension and SS</td>
<td>54% 46% 42% 39% 39% 38%</td>
</tr>
<tr>
<td><strong>1978 ADMINISTRATION PROPOSAL</strong></td>
<td></td>
</tr>
<tr>
<td>Pension only</td>
<td>20% 24% 30% 32% 34% 34%</td>
</tr>
<tr>
<td>Pension and SS</td>
<td>74% 60% 49% 43% 42% 40%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Statute/Proposal</th>
<th>Final Average Pay</th>
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<tbody>
<tr>
<td><strong>Offset Plan</strong></td>
<td><strong>$5000 $15,000 $30,000 $50,000 $75,000 $100,000</strong></td>
</tr>
<tr>
<td><strong>PRE-1986 LAW</strong></td>
<td></td>
</tr>
<tr>
<td>Pension only</td>
<td>5% 20% 34% 40% 44% 45%</td>
</tr>
<tr>
<td>Pension and SS</td>
<td>59% 56% 53% 52% 52% 51%</td>
</tr>
<tr>
<td><strong>1978 ADMINISTRATION PROPOSAL</strong></td>
<td></td>
</tr>
<tr>
<td>Pension only</td>
<td>23% 32% 40% 44% 46% 47%</td>
</tr>
<tr>
<td>Pension and SS</td>
<td>77% 68% 59% 55% 54% 53%</td>
</tr>
</tbody>
</table>

This proposal would have required employers to pay, in general, at least half the amount of benefits to participants with wages below the integration level as they paid employees with wages above the integration level.445 While this proposal clearly established a precedent for the "permitted disparity" integration rules later enacted in the 1986 Tax Reform Act,446 it took a somewhat

445. The proposal would have required that under excess plans, the percentage of earnings replaced above the integration level could not be higher than 2.1 times the percentage replaced below the integration level—the original proposal was 1.8, a figure revised upwards after pressure from employers. *Id.* at 58 n.42. Under offset plans, the offset percentage could not exceed the plan's general wage replacement rate—so that if the plan provided benefits equal to 50% of final pay, the offset percentage could not exceed 50%. *See id.* at 58.
446. *See infra* Part V.D.
simpler approach in attempting to provide something like a minimum benefit level from pensions for low-wage employees. This was an approach essentially designed to produce a specified income result—that is, higher total benefits for low-wage workers from the combination of pensions and Social Security.

Nonetheless, a substantial reduction in benefits through integration would still have been permitted under this provision, reflecting both employer pressure and the prevailing view—even of reformers—that integration was necessary to prevent "overpensioning".447

It is also my opinion that integration with Social Security as now practiced is inconsistent with the special tax benefits for qualified plans... It makes no sense to allow integration if it leads to complete exclusion of the low paid and limited benefits for the middle income group.

On the other hand, if Social Security could not be taken into account, it would be impossible for an employer to provide a pension adequate to replace pre-retirement earnings for the higher paid without giving the lower paid a combined annuity, from Social Security and the private plan, in excess of 100 percent of their income while employed. Thus, integration does have a proper role.448

C. 1986 Tax Reform Act: "Permitted Disparity"

The 1986 Tax Reform Act,449 following the rejection of the 1978 Carter administration proposals, contained the first substantial revision to the statutory rules governing integration since the 1942 Revenue Act.450 Most critics of integration approached the tax reform debate from the perspective either of retirement income adequacy needs or simple fairness to low-paid workers. Most proponents of integration based their arguments on the need to prevent "excess" replacement rates at low-income levels from the combined benefits of Social Security and private pensions.451

447. See Altman, supra note 86, at 494-95.
448. Halperin, supra note 86, at 762.
The 1986 Act revisions, however, did not satisfy either camp; as discussed below, the changes fell short of eliminating integration altogether while still attempting to eliminate or severely limit the ability of employers to neutralize the effect of income redistribution under Social Security. The errors lay in two areas: first, the assumption that integration was necessary to prevent "excess" replacement rates from the combination of Social Security and private pensions; and second, the determination that the best way to limit integration's effects was to model a solution on the IRS approach of determining an "employer share" of the Social Security benefit.

1. Framing the problem: 1986 Senate hearings

The positions of the parties involved—employers, pension advocates, and organized labor—were clearly articulated in a series of hearings held by a subcommittee of the Senate Finance Committee in January 1986.452 While this subcommittee did not have direct legislative jurisdiction over the tax bills that would inevitably contain any substantive pension reforms, many of the concerns expressed at this hearing are reflected in the later Senate version of tax reform which in many aspects prevailed in conference with the House in the summer of 1986.453

The proposed legislation, Senate Bill 1784,454 would have revised the then-current integration rules by imposing limits on integration to produce at least one-half of a nonintegrated benefit for workers in integrated plans, thus focusing on the goal of ensuring at least some pension benefit for low-income workers.455 In testimony before the subcommittee, advocates for pension recipients and workers generally supported the proposed changes on the grounds that they provided adequate retirement income to low-wage workers.456

On the other hand, employer representatives generally op-

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455. See Hearings on S. 1784, supra note 452, at 31-36.
456. See id. at 219-21 (statement of Anne Moss, Deputy Director, The Pension Rights Center); see id. at 234 (statement of Dr. William S. Hoffman, Director, Social Security Department, United Automobile Workers of America).
posed additional limits on integration that might result in replacement rates in excess of 100% from a combination of Social Security and private pensions for low-wage workers. Other industry representatives, notably those speaking for small business, focused on the cost to business created by limiting integration:

These limits [in the proposed legislation] simply do not recognize a corporation's Social Security expense. BellSouth believes that an integration method based on the employer's Social Security contribution is a better alternative. . . . In an offset plan, the accrual could be reduced by the employer's contribution to Social Security or, at a minimum, by the Old Age Survivor portion of the employer's contribution.

S. 1748 seeks to relieve financial pressure on the Social Security System and so eliminates the ability of an employer to integrate a qualified pension with social security for all employees whose earnings fall below the Social Security wage base. . . . As a result of the proposed legislation, an employer may suddenly find that he or she is paying a substantial amount of money on behalf of each employee for two mandated retirement systems. The employer shoulders the burden of funding both systems while the employee remains free of any responsibility.

The employer perspective is clearly delineated in this testimony. Social Security was viewed as a substitute for private pensions, one for which employers were already paying, and represented a cost for which they should be allowed to take credit in providing benefits in their private plans.

2. 1986 Tax Reform Act: House, Senate, and conference solutions

While the pension and benefit provisions of H.R. 3838—the House version of the Tax Reform Act of 1986—were a major focus of staff attention, as well as some members of Congress, the inte-

457. See id. at 141-42 (statement of Edward O. Handy, Jr., Member, Board of Directors, ERISA Industry Committee); see id. at 313 (statement of the American Council of Life Insurance).
458. Id. at 373 (statement of BellSouth Corporation).
459. Id. at 504-05 (statement of the National Federation of Independent Business).
gration rules were not a principal focus of the Bill. However, integration provisions were ultimately included in both the House and Senate Bills, principally a requirement in the House Bill that the total integration percentage be accrued ratably over forty years and a more extensive provision in the Senate Bill that would have: (1) reduced the permissible offset percentage to 50% of the pension benefit otherwise due—as opposed to setting a percentage of PIA to set against the pension benefit; and (2) limited the step-rate excess percentage above the integration level to two times the percentage accruals below the integration level.

The distinctions between the House, Senate, and conference versions are chiefly technical. While both versions would have retained integration as a permissible exception to the nondiscrimination rules, both attempted to limit the amount by which a low-wage or short-term worker's benefits could be reduced. The House Bill accomplished this by forcing ratable reductions based on an integrated formula, effectively protecting short-term workers from complete elimination of their pension benefits. The Senate Bill took a more direct approach, simply requiring that at least 50% of the accrued pension benefit must be paid, regardless of the offset that would otherwise result from an integrated formula.

In the Joint Committee on Taxation report prepared to document the final conference agreement reached on August 16, 1986, only brief descriptions of the agreement reached by the conferees were included, leaving the details and statutory language for staff to work out over the congressional recess. The entire explanation of the tentative agreement is as follows: "[The] House recedes with simplified rules to limit disparities to levels comparable

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460. The major impetus for the specific legislation that became the Tax Reform Act of 1986, the Treasury Report to the President, Treasury Department's Tax Reform for Fairness, Simplicity, and Economic Growth, released November 27, 1984, contained major proposals for revising the nondiscrimination rules for private pensions but no recommendation concerning integration. H.R. 3838, the House Bill version of the 1986 Tax Reform Act, did contain a modification to integration, as discussed below, but the overall thrust of tax reform was generally to broaden the tax base and dramatically reduce tax rates. See H.R. 3838, 99th Cong. § 101 (1985).


462. See id. at 432-35.

463. See id. at 431.

464. See id. at 432-35.

to disparities permitted under present law and with rules providing for accrual of such disparities.\textsuperscript{466}

The staff, including the House Ways and Means Committee, Senate Finance, Joint Committee on Taxation, Treasury, and IRS staff, proceeded to spend the next month developing the most extensive change in integration rules since 1942.\textsuperscript{467} The final conference report in September described the conference agreement as generally following both the House Bill and the Senate Bill with certain modifications. Most importantly,

in order to limit the extent to which an employer may increase, relative to the present law integration rules, the disparity between benefits accruing with respect to compensation above and below the integration level, additional limits on such disparity are applied . . . .

The additional limits . . . on the permitted disparity are a simplified form of the present-law integration rules, modified to eliminate the need for offset plans to determine an employee's actual lifetime social security benefit, provide for parity between offset plans and excess plans . . . . and eliminate the adjustments for integrated ancillary benefits (except for early retirement benefits).\textsuperscript{468}

One principal aim of the staff was to make the integration rules more consistent with the current social security benefit structure and to prevent employers from taking credit for the whole weighted portion of the social security benefit that goes to low-income employees. We did this by limiting the reduction in employee pensions to an amount equal to the employer-provided portion (essentially one-half) of the social security benefit paid to a worker at just below aver-

\textsuperscript{466} Id.


\textsuperscript{468} See H.R. Conf. Rep., supra note 461, at 435.
The legislation substituted the concept of “permitted disparity” between low- and high-wage workers in a formula taking account of Social Security benefits or contributions with the older concept of substituting Social Security benefits for private pension benefits for low-wage workers. In this way the principle was established that a 100% offset of pension benefits with Social Security benefits was not permissible.

At the same time, the permitted disparity concept further reinforced the comparative approach of the nondiscrimination rules generally by allowing substantial, but not “excessive,” differences between pension benefits based on an “unweighted” Social Security benefit. In other words, the concept was to allow employers credit for some portion of the Social Security benefit—that portion that could be said to be a substitute for what they would have provided in the pension benefit in the absence of Social Security, a strictly proportionate benefit. But employers were not to be allowed credit for that part of the Social Security benefit that went beyond proportionate to redistributive.

In general, then, section 401(l) was based on the same misapprehension about the nature of the relationship between employer contributions and Social Security as the IRS’s long history of rulings had been based on. In accepting the premise that an “employer-provided portion” of the Social Security benefit existed, the legislation inevitably produced a level of integration that might be lower for some low-wage workers but that nonetheless perpetuated the violation of entitlement principles inherent in integration.

D. 1986 Act Analysis: Was the Game Worth the Candle?

Despite the fears expressed at the time of the 1986 Tax Reform Act, the death of integration has been greatly exaggerated.

469. Confidential memorandum from Patricia Dilley to Rob Leonard, Chief Tax Counsel, Committee on Ways and Means (Sept. 16, 1986) (on file with the Loyola of Los Angeles Law Review).
471. See id. § 401(l).
472. See id.
473. Industry representatives expressed surprise and even outrage at the new rules, while commentators immediately began developing technical problems created by the new statute, most of which surfaced in the process of development of successive sets of regulations. See infra note 474.
In fact, as more stringent nondiscrimination rules are put in place, the use of integration to preserve existing benefit and contribution formulae that would otherwise be discriminatory may have stayed constant, despite the limits placed on integration itself.

Since the effective date for the provision was repeatedly delayed pending development of implementing regulations,\textsuperscript{474} there is limited data on the actual impact of the new integration regulations. In theory, several problems can be identified, particularly the extent to which integration can still be used to severely reduce benefits for low-wage workers.\textsuperscript{475} Nonetheless, an analysis done by the Congressional Research Service (CRS) in 1994 concludes that the 1986 Act modifications accomplished a principal goal: to prevent elimination of private pension benefits for low-wage and short-service workers.\textsuperscript{476}

While benefits can still be reduced through the use of the permitted disparity rules, the new law ensures that employees vested in an employer pension plan will receive at least some pension benefits.\textsuperscript{477} Nonetheless, despite the fact that the 1986 Act appeared to have influenced plan sponsors to change their integra-

\textsuperscript{474} After a series of proposed regulations were raised based on public comment, final regulations on all the nondiscrimination rules were issued on September 12, 1991, but then were further amended and issued in final form on August 31, 1993. While the 1986 Tax Reform Act provisions were effective for plan years beginning after 1988, the final regulations were effective for plan years after 1993. The regulations state that a good faith compliance standard would be applied in the interim. See Treas. Reg. § 1.401()-6-(a)-(L) (1991).

\textsuperscript{475} While praising the 1986 rules as simpler and as channeling more pension benefits to low-paid workers, Altman severely criticizes the legislation for retaining the basic concept of the integration level and for replacing “the current integration rules with mechanical rules lacking any conceptual basis.” Altman, supra note 86, at 488. She demonstrates that workers just above the integration level may end up with a lower total replacement rate than workers lower on the income scale and states that if the employer wishes to raise benefits for the middle-income worker, total replacement rates for the low-paid worker would have to approach 100%. See id. at 490-92. While there is substantial merit to Altman’s complaints about the 1986 Act, there are two basic problems with her approach. First, with respect to her critique of the 1986 Act, much of the disparity in total replacement rates between people very close on the wage scale appears to be an outgrowth of the integration level itself, as Altman points out, and not a result of the 1986 Act revisions. See id. at 489. More importantly, her criticism would have been more telling if she had discussed more fully the .75\% excess allowance percentage, since the basis for it was acceptance of the proposition—fundamental to integration in general—she so roundly criticizes elsewhere in the article, namely, that employers pay for half of Social Security benefits and should be given credit for it.

\textsuperscript{476} See KOLLMANN ET AL., supra note 431, at 15.

\textsuperscript{477} See id. at 5.
tion methods from offset to excess, the CRS study also concludes that as of 1991, 54% of all pension participants were still covered by integrated plans.

The CRS study also compares the replacement rates achieved by long-term workers under nonintegrated plans with the results under plans integrated under the old law and under the 1986 Act provision. For workers with thirty-five years of service under a typical nonintegrated plan allowing accrual of benefits equal to 1% of final average compensation for each year of service, the combination of Social Security and the private pension benefit results in total benefits equal to 120% of final earnings of $5000. Given that only 8% of full-time workers earning under $10,000 per year are covered by a pension plan at all, this replacement rate in excess of 100% seems unlikely to be a very common phenomenon.

For workers with final years’ earnings of at least $7500 or higher, total income replacement in a nonintegrated plan falls below 100%, equaling around 80% for final earnings around $20,000 and gradually declining to 48.4% for final earnings of $95,000. In comparison, for workers covered by a typical offset integrated plan—allowing only a partial offset against the Social Security benefit—the new law would provide slightly higher replacement rates than the old law would have for workers earning less than $10,000. In other words, the new law would have no effect at higher earnings levels under offset plans. However, for plans taking maximum advantage of the integration formulae allowed under both old and new law, the new law could result in substantially higher replacement rates particularly for low-paid workers but also potentially for high-wage workers.

In summary, the permitted disparity rules may reduce the maximum benefit reductions allowed by pension integration, but it seems unlikely that the new formula will affect most workers at average wage levels under more typical integrated plans. Nonetheless, the most serious problem with the approach of the 1986 Act lay not in its technical details but in its fundamental assumptions. The stated aim of the staff in developing the 1986 Act approach of “permitted disparity” was based on the idea that an accurate measure of the portion of the Social Security benefit that employers “paid” for, apart from the social benefit of redistribu-

478. See id. at 7.
479. See id. at 8.
480. See id. at 9.
As discussed above, however, the financing of Social Security is functionally unrelated to benefits paid under the system, and thus the technical structure of the permitted disparity rules is built on a serious theoretical misapprehension. While the new rules probably improve the end result for lower-paid workers in comparison with pre-1986 law, the premise is no less flawed than the basis for the original integration provisions.

In addition, as shown by the CRS data, so few workers at the lowest wage levels are likely be covered by private pensions that the goal of preventing excess replacement rates from the combination of Social Security and private pensions seems hardly worth pursuing even if one accepts the premise that a final replacement rate percentage should be imposed on that combination. More importantly, integration, even as modified by the 1986 Tax Reform Act, presents an inescapable contradiction to the principle of entitlement by allowing a loophole out of the nondiscrimination rules that would otherwise guarantee workers a full pension benefit in addition to their Social Security benefit.

VII. CRITIQUE OF INTEGRATION: ENTITLEMENT PRINCIPLES, POOR RELIEF RESULT

After over fifty years of debate and attempts at repeal, the integration rules are still a widely used feature of the nondiscrimination regime. The critiques of integration tend to fall into two categories: those based on adequacy of retirement income and those attacking the argument that employers "pay" for Social Security. While both types of criticisms are valid, there are counter arguments to each that are relied on by employers and many pension analysts to preserve integration in the face of legislative change. Both critics and defenders have based their arguments essentially on the results of integration; neither side has focused on the essential entitlement principles of Social Security with which integration is fundamentally inconsistent.

Some pension experts have continued to call for revision of the integration provisions for a variety of reasons summed up by the CRS study of integration:

While integration reflects the employer's cost of social security and serves to minimize the cost of providing a voluntary private pension, it also has the practical effect of partially or totally denying private pension benefits for
individuals whose earnings are below the social security wage base.

... [T]he concept of integration raises questions of equity toward the lower and moderate wage earner.

The view that social security benefits attributable to employer taxes are, in effect, part of the employer's private pension plan can be questioned. Yet, this is the rationale behind the Internal Revenue Service's derivation of the integration guidelines. Indeed, many economists state that workers as a class bear the ultimate cost of social security contributions (and even the cost of private pensions, for that matter).

... To the extent that integration procedures reduce private pensions of individuals with low and moderate incomes, these procedures may be deemed to frustrate the intent of social security increases provided by Congress.481 Yet even critics of integration concede that a problem of "excess replacement rates" from the combination of Social Security and private pensions still exists: "However, if social security benefits were not considered in establishing private plan benefit formulas, the income replacement rate from combined public and private benefits might exceed 100 percent for certain lower wage earners."482 The solution supported in the CRS paper logically results from focusing on income targets with a view to assuring adequate but not excessive income in retirement:

[T]he integration guidelines could be based upon some congressionally approved income replacement objectives, that (a) would assume a Federal responsibility to provide a certain standard of income replacement at various income levels through a public system, and (b) would offer tax incentives for the private pension system to supplement the public system up to certain maximum levels. Low-wage earners may be found to need practically 100 percent income replacement, with the rate gradually decreasing as income increases. Higher income individuals who wish to make up the difference between their preretirement income and the congressionally defined stan-

481. Paper No. 18, supra note 374, at 186.
482. Id.
standard of combined public and private income replacement could do so through voluntary saving.\textsuperscript{483}

This proposal, like most other reform proposals, focuses on providing some measure of “adequate” income for all workers from the combination of Social Security and private pensions. Such a focus tends to downplay Social Security’s role in redistributing income, apart from assuming that private pensions have a smaller part to play in achieving an adequate replacement rate for low-income workers.

Nonetheless, if the role of redistribution is important to the success of Social Security in assuring, and perhaps inducing, mass retirement and maintenance of above-poverty level consumption in retirement, any integration “solution” must preserve it. Thus, before addressing the shortcomings of the various standard critiques of integration, it is necessary to turn to the question of redistribution itself and whether Social Security’s redistributive effect is significant enough to be concerned with.

A. The Problem of Integration and Social Security Redistribution

During the postwar period Social Security was greatly expanded in coverage, as described above, and benefit levels continued to increase.\textsuperscript{484} By the 1960s retirement was firmly entrenched in the working life-cycle, and most Americans expected and planned to retire by age sixty-five, if not earlier.\textsuperscript{485} In fact, labor force participation rates of men over age sixty continued to decline into the 1990s to the point that age sixty-five was only a theoretical retirement age for most workers who preferred to retire at age sixty-two or even earlier. The end result of the expansion of Social Security was a greatly enlarged role for the program in assuring retirement income for almost all workers at all points of the wage scale, except for the highest paid whose Social Security benefits would continue to be quite small in comparison with their earnings.

The redistribution in the Social Security benefit formula can be demonstrated by looking at the initial benefits payable to workers at various income levels. The following table compares the Social Security PIA, which is the basic age sixty-five retirement

\begin{table}[h]
\centering
\begin{tabular}{|c|c|}
\hline
Income Level & Initial Benefit \hline
Low & Small \hline
Middle & Medium \hline
High & Large \hline
\hline
\end{tabular}
\caption{Social Security Benefit Comparison}
\end{table}

483. \textit{Id.} at 188.
484. \textit{See} MYERS, \textit{supra} note 34, at 229-371.
485. \textit{See}, e.g., ACHENBAUM, \textit{supra} note 122, at 105-08 (discussing the establishment of 65 as the benchmark retirement age by 1960).
benefit for workers at low, average, and maximum lifetime earnings, and the replacement rates for each.

<table>
<thead>
<tr>
<th>Retirees in January 1994</th>
<th>January 1994 PIA</th>
<th>Replacement Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low earner (45% of average earnings)</td>
<td>$ 505.30</td>
<td>57.4%</td>
</tr>
<tr>
<td>Average earner ($23,532 in 1993)</td>
<td>$ 829.80</td>
<td>42.4%</td>
</tr>
<tr>
<td>Maximum earner ($57,600 in 1993)</td>
<td>$ 1147.50</td>
<td>24.0%</td>
</tr>
</tbody>
</table>

These figures show the theoretical degree of redistribution in the Social Security benefit formula—obviously the lower the average wage, the higher the replacement rate. If the effect of family benefits is added in, replacement rates for the low-wage earner can approach 90%, while the maximum earner's rate increases only to about 35%. Thus, low-wage workers clearly receive more than a strictly proportional benefit, and high-wage earners receive a less than proportional benefit. Even for low-wage earners, however, Social Security provides only a base of income with a substantial role left for private pensions and savings to play in assuring adequate income in retirement, except in the case of a lifetime, extreme low-wage worker with dependents receiving benefits; such a family might receive close to 100% replacement of pre-retirement earnings from Social Security alone.

Recent economic studies have focused on the reality of this theoretical redistribution, questioning whether the earnings basis of the system has undercut redistributive goals. One such recent study, for example, proposes to analyze how Social Security redistributes income by focusing on the "return" to workers of the FICA tax contributions made to Social Security by them and their employers in order to determine how much redistribution occurs from a "lifetime" perspective:

A more thorough understanding of Social Security's redistributive nature requires moving to a lifetime perspective, that is, examining how Social Security benefits actually compare in value with tax contributions over a
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lifetime for people of different generations, income levels, and family types. . . . Our approach . . . involves using standard actuarial procedures to compare the value of the annuity provided by Old-Age and Survivors Insurance with the value of a private annuity or pension that could be purchased with a worker's lifetime OASI contributions. 486

This approach is based on the premise that the most accurate measure of redistribution is the "net-transfer"—which compares taxes paid into the system with benefits paid out over a lifetime to each beneficiary:

A positive net-transfer—the difference between lifetime benefits and taxes—means that an individual or family receives a subsidy above and beyond the fair annuity value of contributions, whereas a negative net transfer indicates that benefits are worth less than contributions. Those with positive net transfers have lifetime income redistributed toward them, while those with negative net transfers have lifetime income redistributed away from them. 487

The conclusion reached by most analysts using this definition of redistribution is that Social Security is most "redistributive" for the generation currently receiving benefits since their contributions into the system—plus earnings on those contributions—could not have provided an annuity equivalent to their current benefits. 488

This analysis maintains that Social Security has been "regressive" in distribution of income within generations of workers: "within a given cohort of retirees, net transfers have been inversely related to need: people with the highest lifetime incomes have tended to receive the largest absolute transfers above and beyond what they contributed." 489 While the author concedes that the progressive benefit formula does provide a "higher rate of return on contributions" 490 for low-wage earners, he points out that because benefit levels rose so substantially through 1977, and are indexed for inflation, the benefits accruing to high-wage workers are in absolute dollar terms much higher than a progressive benefit

487. Id. at 1767.
488. See id. at 1767-69.
489. Id. at 1768.
490. Id.
The comparative level of redistribution to low-wage workers is counterbalanced by the sheer size of benefits received by high-wage workers under the proportional formula.\textsuperscript{492}

The essential flaw in this "return on investment" analysis is the supposition that a public entitlement system should be evaluated just as a private pension system might be—by comparing tax payments to benefit returns. In such an analytical framework, an earnings-based entitlement is recast into a contribution-based entitlement, and is evaluated according to its ability to fulfill whatever objective is most important to the analyst. A benefit structure tied to earnings levels will necessarily produce higher benefits for high-wage workers even though it might pay higher than strictly proportional benefits to low-wage workers. Thus, any earnings-based benefit system must inevitably fall short when viewed in such a framework, whether the goal is redistributing income to the low-wage workers or providing an adequate "rate of return" on contributions by high-wage workers.

This framework, however, misses the essential point of earnings-based public entitlements, which is to provide the assurance of minimally adequate benefit payments in order to induce retirement, an assurance which, given the history of the American retirement income system,\textsuperscript{493} can only be based on a right that is earned, regardless of how it is paid for. Again, the "money's worth" analysis confuses the contributory financing system with the earnings basis for benefit payments, mistaking the symbolic function of FICA tax contributions as a representation of the work by which a beneficiary earns his or her entitlement for a literally contributory pension scheme.

As discussed above, the contributory financing structure was intended in large part to limit funds available to spend on Social Security benefits in order to stave off successive increases in benefits such as had been enacted for the Civil War pension system.\textsuperscript{494} However, FICA tax contributions by workers represent more than a limited source of revenue for benefits—the payroll tax system serves as a tangible representation of earnings upon which entitlement to benefits is found, performing a dual function of financ-

\textsuperscript{491} See id.
\textsuperscript{492} See id. at 1768-69.
\textsuperscript{493} See discussion supra Parts III-IV.
\textsuperscript{494} See discussion supra Part IV.
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ing benefits while also communicating worthiness.

The proper measure of redistribution is not how contributions compare to benefits but instead how the benefits paid out to low-wage workers compare to the level of income needed to maintain an independent life in retirement, at an income level comparable to—or even improving on for those at the bottom of the wage scale—the income level while working. This is, after all, the point of redistribution to begin with. Under this measure, as well, the redistribution of the Social Security benefit formula may fall short of some standard of adequacy, indicating that perhaps some increase in the progressivity of the benefit structure is in order.

However, given the fundamental point of Social Security and private pension entitlement—which is that individually earned rights are the only legitimate basis for entitlement—insufficiency or surplus of income in retirement is generally a consequence that must be addressed through programs outside the entitlement system—needs-based benefits to supplement insufficient income or higher progressive tax rates to reduce surplus income. Pension integration, in contrast, seeks to address one possible consequence of redistribution—surplus income in retirement from the combination of pensions and Social Security—through a consequence-based system without regard for entitlement principles.

B. Integration and Adequacy of Retirement Income

Critics of integration have frequently proceed from the basic precept that private pensions should be combined with Social Security to produce adequate total retirement income and that integration undercuts that goal. The prospective redistribution of the Social Security benefit formula provides a cushion to make up for deficiencies that are likely to exist upon retirement because of low wages, low pension amounts among them. Therefore, redistribution cannot be considered a substitute for pensions for low-wage workers—the weighting in the benefit formula barely serves to compensate for lack of personal savings because of lack of surplus income.

While the adequacy concern is important and these arguments are valid, they are usually countered fairly easily by the argument that private pensions are not designed to be antipoverty programs

495. See, e.g., Hearings on S. 1784, supra note 452, at 219-21 (testimony of Anne Moss, deputy director, Pension Rights Center).
and that the task of ensuring adequacy is better met by needs-based programs. The more compelling critique of integration lies in its origin rather than its consequences.

Pension integration undercuts a principal goal of social insurance, which is to provide a predictable benefit amount based on past earnings, not current need, in order to assure workers even at lower income levels that they will have an income cushion if they voluntarily retire. This scheme is essential to the labor management function of social insurance—providing assurance to workers that work even at low wages will have its reward in adequate retirement income.

More broadly, redistribution itself becomes a kind of second level of social insurance—insuring against long periods of unemployment or years out of the work force for child rearing or education by giving higher proportional benefits to all those with low average lifetime wages. The prophylactic antipoverty elements of Social Security, as discussed above, were inextricably linked from the beginning of the program to its "earned right" status: entitlement and earnings, retirement and redistribution, were all part of one package.

C. Integration and the "Employer Share" of Social Security

Proponents of integration argue that employers should be able to treat their contributions to Social Security as part of their employees' overall retirement income package, thus reducing private pension benefits to take account of Social Security, which they have "paid for" through FICA taxes. Of course, this view is questionable in light of the commonly accepted economic view that private pensions represent a trade-off made by current workers in the form of lower current pay in exchange for pension benefits upon retirement. More importantly, this "employer credit" rationale is based on the premise that Social Security is another type of employer-provided, or at least partly employer-provided, pension that private employers are fully justified in taking account of in providing for their employees.

The response to this claim is usually that since current FICA taxes pay for current retiree benefits on a pay-as-you-go basis, employers cannot claim they are paying for part of their current

496. See MUNNELL, supra note 46, at 14-15.
497. See id. at 7-29.
work force's retirement income.498 Moreover, in the markedly less stable working environment today in which employees move from job to job over their lifetimes, the relationship between any one employer's FICA tax payments and a particular worker's ultimate Social Security benefit is tenuous at best.

While both of these arguments are valid, they are vulnerable to the counter argument that since intergenerational shifts of productivity from the working to the nonworking are inherent in any retirement income system, public or private, employer FICA contributions today are simply a proxy for the FICA contributions of tomorrow that will actually fund employee retirement benefits. From that perspective, each cohort of employers is paying for the last cohort of workers—and since the payments would be similar in present value terms, the employer might still have a valid argument in favor of integration.

The real problem with this argument, however, is that the individual relationship upon which private pensions are based creates a very different type of entitlement than that created by the "social compact" on which Social Security is based. Private pension benefits are grounded in the relationships and promises made between employer and employee—a one-to-one relationship. In contrast, Social Security benefits are grounded on the relationship between the working and the nonworking and on promises of social support based on a past history of productive employment—a "many-to-many" relationship.

Moreover, employee entitlement in Social Security benefits is not based on contributions but on earnings.499 Employee contributions serve as a visible metaphor for earnings upon which benefits are based, but both employees and employers finance the system through FICA tax contributions that are not directly related to any individual benefit amount.500 Thus, the presumption underlying pension integration—that employers should get "credit" in their private pension relationship for contributions to the public program—is per se invalid. In financing the Social Security system, employers are not paying for specific benefit amounts for any specific set of employees. They are in reality paying for redistribution generally.501

498. See, e.g., SCHULZ, supra note 190, at 157-62.
499. See discussion supra Part VI.
500. See discussion supra Part VI.C.2.
501. If one assumes the employee bears the entire FICA tax burden, employers
D. Integration and "Overpensioning"

A final argument in defense of integration is that integration is a necessary mechanism to ensure that low-wage workers do not receive "excessive" retirement income from the combination of Social Security and private pensions. This offshoot of the "adequacy" rationale essentially argues against "overpensioning" on the assumption that the goal of the retirement income system—Social Security and private pensions together—should be to provide a relatively uniform level of retirement benefit, expressed as a percentage of the worker's earnings level while employed to workers at all wage levels, albeit with somewhat higher benefits going to low-wage workers.

Such a view rests on the notion of fixed replacement rates. Pension analysts usually assume that workers need to receive retirement income equal to a fixed percentage of pre-retirement earnings—frequently set at 80%. Therefore, integration is seen as a way to arrive at the proper replacement rate by a combination of Social Security and private pension benefits, resulting in largely public entitlement income for the low-paid and largely private entitlement income for the more highly paid.

From this perspective the redistributive features of Social Security are viewed as permitting employers to provide lower or no pension benefits to low-paid workers on the grounds that these workers are taken care of by the public system. Thus, in this framework, the overall retirement income security system is appropriately tiered: (1) Social Security provides total or a higher portion of retirement income for the worker below the wage base; (2) private pensions provide most income for the highest-wage workers whose Social Security benefits make up an insignificant portion of total retirement income; and (3) middle income workers receive a more equal mix of Social Security and private benefits.

One problem with the overpensioning argument is that very few workers run much of a risk of excess retirement income from the combination of Social Security and private pensions, and those that do are likely to be extremely poor, as the CRS study discussed

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503. Altman's "worker security proposal" is essentially based on this premise.
504. See Schulz, supra note 190, at 95-97.
above demonstrates. The prospect of replacing more than 100% of pre-retirement income of such workers with a combination of Social Security and private pensions is hardly alarming. Those few full time workers for whom such replacement would be possible would necessarily have lifetime earnings so far below the poverty level that some sort of subsidy in retirement, either through Social Security or a direct means-tested program, would be inevitable.505

Perhaps more importantly, there is another possible view of the proper relationship between Social Security and private pension entitlements that produces a different conclusion about the function of redistribution in Social Security. After fifty years of expansion to nearly universal coverage of the work force, Social Security should more accurately be seen as a universal entitlement for all workers in an economy built around the expectation of retirement. From this perspective, the system’s redistributive function becomes more important, insuring workers in retirement against not just inability to work in old age but also against the hazards of periodic unemployment or underemployment, inadequate education, and a host of other circumstances throughout their lifetimes that may result in inadequate income in old age.

Under this view, the private pension system’s role is to provide additional retirement income to all employees—in essence, preserving the redistribution inherent in the Social Security benefit formula and allowing workers to add whatever additional amounts they can through private pensions and savings. The prospective nature of Social Security’s redistribution combined with the entitlement character of the benefit means that even the poorest workers with an excess replacement rate would have a claim on retirement income relatively free of state intrusion into their current economic state. This preservation of autonomy and control, even in the context of a government subsidy, is what Social Security redistribution was intended to provide and what pension integration undermines.

Pension reformers have been primarily concerned with designing a public-private retirement income combination that would ensure provision of adequate but not excessive replacement rates.506

505. See discussion supra Part VI.
506. See discussion supra Part VI. Prior to the extensions of Social Security Coverage in the 1983 Social Security Amendments, many analysts viewed overpensioning as a legitimate problem, because workers earning a government pension designed to serve as a combination Social Security/private pension could work a
As a result, their suggested integration reforms were necessarily based on indirect means-testing, just as integration itself is through the use of targeted replacement rates. Such an approach violates the essential principles of entitlement and freedom to accumulate represented by both Social Security and private pensions. A “worker security” goal of insuring that low-wage workers have sufficient retirement income appears to be inevitably accompanied by a corresponding concern that such workers not receive “too much.” Yet it is precisely this need assessment and income control that old-age entitlements, from Civil War pensions to Social Security, were intended to avoid.507

One alternative integration scheme, from a worker security perspective, is to pick a target replacement rate for income at retirement and allow employers to integrate plans with Social Security only by subtracting the Social Security PIA from the target replacement rate, with the private pension making up the difference.508 Such an approach would eliminate the notion of employer-provided portions of Social Security from integration and would focus the retirement system on combined income replacement from both private and public systems. “The law should permit qualified private pension arrangements to be integrated with Social Security in only one situation. That situation is when, without coordination, benefits from Social Security and qualified retirement plans in combination will result in overpensioning a segment of the work force.”509

Thus, even this “worker security” framework would involve some form of integration to prevent “excess” earnings replacement consistent with most analyses of integration emphasizing economic results, rather than principles of rights or entitlements that workers earn under both public and private systems.510 Such proposals have typically been based on a well-meaning but ultimately manipulative concern for assuring sufficient, but not “excessive,” income maintenance for poor and middle-class workers. The question, of course, is why the possibility of excess re-

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507. See discussion supra Parts III-IV.
508. See Altman, supra note 86, at 496-97.
509. Id. at 495.
510. See discussion supra Part V.
placement rates has overridden fundamental entitlement principles as the primary policy concern.

Excess replacement rates for workers with lifetime minimum-wage earnings appear to present an essentially moral problem. Some analysts believe that the work disincentives inherent in receiving retirement income that exceeds working income require some level of integration to reduce the excess total, despite the probability that workers meeting this profile most likely had inadequate wages throughout their working life. However, even when the focus is on results rather than basic principles, it is not at all clear why excess replacement rates should be considered a problem for the low-wage Social Security beneficiaries who might receive them.

Without other sources of income, workers who could achieve these excess replacement rates most likely required poverty-based assistance even while working and could certainly be expected to require it in old age. In 1939 the lifetime low-wage worker, in fact, could have been predicted to be the intended maximum beneficiary of Social Security’s redistributive benefit formula in order to eliminate the need to turn to means-tested, poverty-based benefits in old age.

The key element on which broad-based American retirement income entitlements historically have been founded are worthiness based on service—expanded in Social Security to include work in covered employment—and predictability of receipt in old age. Income targets, whether indirectly through means-tested poverty programs or total replacement rate targets to be met by a combination of Social Security and pension benefits, contradict this fundamental goal.

A “worker security” standard requires imposition of a retirement income target based on some measure that is simply a synonym for need. In contrast, both private and public earnings-based retirement entitlements, consistent with their roots in American poor law principles, reject the notion of needs-based targets in favor of opportunistic anarchy. A worker security integration plan based on income targets does little or nothing to restore redistribution since the target replacement rate would be set generally at 80% for all income levels, and Social Security and private pensions would simply divvy up the total depending on whether the worker

511. See discussion supra Part VI.
is high-paid or low-paid. The notion of lifting up low-wage workers through the progressive benefit formula to a level upon which they would build pension and savings income is lost in a total replacement rate analysis.

Any worker security approach to integration that concentrates on providing total replacement rates by combining Social Security and private pensions is fundamentally inconsistent with the basic "opportunity to accumulate" entitlement embedded in the Social Security benefit formula. Moreover, allowing employers to eliminate or reduce pensions to which their low-wage workers would otherwise be entitled is a violation of the private entitlement guaranteed those workers by the nondiscrimination rules. Suggestions based on a targeted replacement rate for retirement income are inherently antithetical to the fundamental principle of Social Security: earned entitlement without the imposition of income standards from above.

VIII. CONCLUSION

The history of retirement income entitlements demonstrates that economic rights have historically only achieved political and public legitimacy in the American context when the right in question is created through individual effort. Retirement entitlements are qualitatively distinct precisely because they are completely prospective—the very prospectiveness of the right to consumption in retirement requires an absolute entitlement to be effective. The integration rules developed by the IRS and the changes enacted in 1986 were a technical response to the political and philosophical problem at the heart of retirement: how best to assure the prospective income support for mass retirement for a population with increasing life spans in a dynamic capitalist economy.

Social Security was the embodiment of the American tradition of income support for the deserving elderly in which individual autonomy and freedom from control by poor relief authorities was earned by certain, but not all, categories of the elderly. This effort to preserve the worthy from poor relief had its roots in English Poor Laws, developing most clearly in the Civil War pension system for veterans and their families. The perception of who was deserving—that is, who had "earned" a right to income that would prevent poverty in old-age—gradually broadened from needy and

512. See discussion supra Part III.
disabled veterans to aged veterans to those who had worked for at least a substantial part of a lifetime.\textsuperscript{513}

The prophylactic function of earned-right pensions—to prevent reliance on poor relief or the almshouse—can be clearly discerned in the line of public pension programs that began with Revolutionary War pensions.\textsuperscript{514} The real distinction between Social Security and its predecessors was its role in institutionalizing retirement, along with the expectation of income support in old age, in order to meet the needs of an advanced industrial economy that was perceived to have more economic output than jobs.

Social Security represents a recognition of a social responsibility to ensure mass retirement in light of the social and economic role that retirement came to play by the mid-twentieth century in labor force management. While individuals were always assumed to have principal responsibility for providing for themselves, Social Security was a way of mediating that responsibility to take account of economic cycles that might render individual effort meaningless or inadequate as had occurred in the Great Depression.

All retirement income entitlements, private or public, are essentially designed to assure workers that they can stop working without fear of destitution. Antipoverty programs aimed at the elderly poor have little or nothing to do with the phenomenon of retirement. Social Security and employer-provided private pensions, on the other hand, were developed in order to support and encourage the decision to retire on a mass scale for workers at all income levels. Social Security was not intended to change the distribution of wealth in American society generally but rather to preserve it.\textsuperscript{515} The low level of benefits ensured a continued large role for individual arrangements and opportunity to augment income in retirement. Nonetheless, redistributive elements of Social Security—the weighted benefit structure and the family benefit payments—were a necessary part of the assurance that at least minimally adequate income would be available in retirement without reliance on poor relief.

However, given the deliberately low level of benefits provided under Social Security, the retirement inducement could only be effective if workers expected to be able to add to their public benefits through pensions, savings, and investments to whatever extent

\textsuperscript{513} See discussion supra Parts III-IV.
\textsuperscript{514} See discussion supra Part III.B.
\textsuperscript{515} See discussion supra Part IV.C.
chance or effort would permit. The entitlement structure of Social Security embodies widely held liberal, democratic capitalist beliefs in economic opportunity and individual responsibility in the context of shared risk. The entitlement to Social Security benefits is not an entitlement to a specific level of income in retirement but rather entitlement to a predictable base of income plus the opportunity to accumulate.

The antipoverty aspects of Social Security are essentially an informed gamble. Because redistribution in the benefit formula is based on earnings while working, not on income in retirement, there is a high probability, but not a certainty, that the benefits of redistribution will accrue to workers who will be poor in retirement as they were in their working lives. However, in keeping with American faith in opportunity and distaste for poor relief, workers at all earnings levels are free to better their income positions in retirement because they have the ability to accumulate outside the Social Security system as much or as little additional income or assets that chance or effort affords.

In contrast, targeted income assistance programs are inevitably class-based, static, and manipulative—poor people must be categorized as poor before they can receive assistance, and they are subject to continual control and eligibility determinations from authorities dispensing the aid so that the public can be assured that only the deserving needy receive public relief. This approach to poverty is not a twentieth or even nineteenth century phenomenon; from the English Poor Law to Aid to Families with Dependent Children (AFDC), American public welfare for the poor has centered on determinations of worthiness as well as of destitution.

The American retirement income system, public and private, developed out of a tradition of saving the most worthy elderly—first veterans, then workers—from recourse to poor relief in old age, based on the notion of earned entitlement to benefits that once “earned” would not be subject to judgment or control from authorities.

When mass retirement became a perceived necessity of industrial capitalism in the twentieth century, earned entitlement combined with some redistribution became the natural basis for the retirement expectation. The ideological force behind the Social

517. See GORDON, PITIED BUT NOT ENTITLED, supra note 23, at 37.
518. See discussion supra Parts II-III.
Security entitlement is the American belief in capitalism itself—that effort should and will be rewarded by the marketplace. The innovation of Social Security was to provide a mechanism for some sharing of the risks of that marketplace, a mechanism that was only politically acceptable because its entitlement structure was consistent with the core belief in economic and social mobility.

The private pension system in the United States, on the other hand, developed in the pre-income tax years primarily as a source of capital formation and as a cheap labor tool—a way for employers to encourage stability in their labor forces without actually being obligated to expend much in the way of pensions. Once the income tax was enacted and the tax benefits of private pension trusts began to play a role in employer decisions to establish plans, Congress and the IRS were compelled to address the question of the proper tax treatment for pension plans and of whether employers should be able to get a deduction for funds set aside in a trust that would eventually benefit only the employer or a few highly paid executives. Far from narrowly focusing on tax avoidance, the nondiscrimination rules for private pensions mirrored the values embedded in the Social Security system—that is, if retirement is an expectation of workers at all levels, private pensions should bear some of the burden of that expectation by providing some benefits to low-wage workers.

Pension integration represents an exception that in some cases swallowed the rule of nondiscrimination, based on the fundamentally mistaken premise that Social Security is simply a part of the employer's pension provision for employees and that the employer has in some way “paid” for all or a portion of employee benefits and therefore should be given “credit” in the nondiscrimination scheme for that payment. The contributory financing structure of Social Security is best viewed in relation to benefits as a representation of earnings that are the real basis for entitlement. Yet the emphasis placed on contributory financing, intended to solidify public recognition of the legitimacy of the Social Security entitlement based on individual effort, led to the illusion that the system was really a contributory pension plan in the private pension sense. The entire technical structure of the integration rules is based on this fundamentally flawed perception of the basis of the Social Security entitlement.

Even those who have rejected the “employer share” argument for integration have nonetheless continued to support the notion
that there is some need to coordinate the results of public with private entitlements. The focus of integration critics and supporters alike on providing level replacement rates for retirement income for workers at all levels reveals an unwillingness to live with the consequences of entitlement—that some people may receive more in retirement than they earned while they were working while others might not have enough to maintain their pre-retirement standard of living.

Yet the entire point of entitlement in this context is the freedom of individuals to earn or not earn what they will. Again, it is the faith in economic democracy and opportunity to accumulate that necessitates earnings as a basis for entitlement. The fact that this entitlement is tied to retirement makes the social mechanism of Social Security and the redistribution benefit formula necessary. Social Security redistribution is essential to the public goal of underwriting retirement for low- and middle-income workers, but the right to the benefit must be inviolable and unrelated to income goals if retirement is to occur.

Thus, if both private and public benefit entitlements are respected, there can be no final income goal imposed; target replacement rates for low-wage workers that might justify integration serve as a substitute for the old English Poor Law in the modern setting. Suggestions to base a new coordination of private pensions with Social Security on level replacement rates miss the point of Social Security. As the first tier of broad-based retirement income support for almost all citizens, its benefits are a universally accessible entitlement earned by participation in the labor force, that can only be effective in assuring prospective consumption if it has the same inviolability as private rights.

The effect of Social Security's redistribution for the lowest-income workers is perhaps to improve their retirement income position in order to induce retirement, while allowing further improvement through additional effort that might result in private pensions and savings. Integration contravenes this prophylactic approach to old-age poverty by lowering pension benefits available from one or more of an employee's pension plans. Thus, the entitlement popularly presented as an inviolable and purely private entitlement—the private pension—emerges under examination as an equally mediated right, affected by public policy perceptions of the correct level of income in retirement for low-wage workers.
What, then, would be the result of living with the consequences of rigorously respected retirement entitlement rights, a framework in which pension integration were abolished? One result might be that some low-wage workers would receive more in pension benefits than they earned while they were working. The other result might be the elimination of private pension plans by employers, as has been the perennial threat in face of efforts to limit integration, because of the increased costs of providing the desired level of benefits to high-wage workers while still providing the required comparable benefits to low-wage workers.\textsuperscript{519}

With respect to the first result, it is unclear why such excess replacement of earnings presents a problem. Workers whose earnings were so low throughout life that they would receive such excess retirement income are clearly still at an income level at or near the poverty level and would require public support from some source in any event. One of the major purposes of the Social Security entitlement since its inception has been to prevent the need for poor relief for those elderly who had worked throughout their lives but still did not have sufficient retirement income because of low wages, bad fortune, ill health, periodic unemployment, or other circumstances unrelated to lack of personal effort—worthiness.\textsuperscript{520} It is difficult to see why it is preferable to force this group of the elderly poor to seek the modern equivalent of poor relief instead of receiving both of their earned entitlements—their pensions and Social Security.

With respect to the possible diminution of private pensions, at least a couple of responses are possible. First, we might begin to reexamine the concept of retirement itself as the nature of work continues to radically change and the employer-employee relationship begins to erode. Public retirement entitlements were viewed as necessary to provoke retirement at age sixty-five for a host of economic reasons including labor force management in an industrial capitalist economy, stimulation of consumption, and preservation of social stability in an economy that was not producing employment at levels sufficient to prevent poverty in old age.\textsuperscript{521} While these propositions may still be valid, the wholesale expectation of ceasing work at age sixty-five or even seventy may no

\textsuperscript{519} See, e.g., Revenue Revision of 1942, supra note 367, at 2488 (commenting that the proposal would eliminate all plans except purely savings plans).

\textsuperscript{520} See discussion supra Part IV.

\textsuperscript{521} See discussion supra Part IV.
longer be appropriate—a more flexible approach to work force participation may need to be developed.

Second, we might shift more of the responsibility for providing retirement income to the public entitlement sphere if private entitlements are not available. Private effort alone has never underwritten mass retirement, which is essentially a phenomenon of the last forty years, coinciding with the expansion of Social Security. If employers find the costs of individually established retirement entitlements too high to bear, it may be appropriate to revisit the Social Security benefit structure to increase redistribution to better insure low-wage worker retirement and to raise replacement rates at the middle-income level in recognition of diminished private pension opportunities.

Retirement savings are now a major source of investment capital, so much so that many are calling for transformation of at least part of the Social Security entitlement to benefits into something more like an IRA. The trend toward employer-provided deferred compensation and investment plans such as 401(k) cash or deferred arrangements, which are essentially incentive savings plans, is already evidence that employers continue to view pension plans most favorably as a source of capital formation best designed to leave most of the risk of economic cycles with the individual worker.

Elimination of integration could have the effect of accelerating these trends reducing worker retirement entitlements to the status of private stock portfolios, which might not prove adequate to fund a long life after work. Yet the lessons of the 1930s are still relevant even into the twenty-first century—capitalist economies by their very nature produce both winners and losers with little regard to socially recognized interests of economic and political stability. The evolution of the American idea of entitlement shows that socially mediated responsibility for economic support of the nonworking elderly is neither a new nor an outmoded concept.

In fact, in the face of an increasing elderly population that will reach its zenith in the first decades of the next century as the baby boom generation attains old age, the need for social income responsibility most likely will increase, not diminish. In the American tradition of recognized economic rights earned through personal effort, pension integration is a truly outmoded concept, and discarding it may be a first step toward true retirement income security for the next generation of workers and retirees.