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PHASED RETIREMENT PROGRAMS FOR THE TWENTY-FIRST CENTURY WORKPLACE

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Private institutional arrangements and public policies encourage early retirement and inhibit flexible retirement arrangements that may involve working less than full-time. But if, even in the face of such disincentives, the employer and employee wished to negotiate a more gradual transition out of the labor force, they would face a number of discouraging legal and regulatory hurdles that were created in the past with the best of intentions.

The notion that our laws and regulations should be designed to facilitate phased retirement represents a 180-degree shift in traditional benefits thinking. For decades, employers have looked for benefits tools to ease older workers *out* of the workforce, either to implement downsizing or to make room for the huge cohort of baby boomers who were eager to work their way up the career ladder. Consequently, there is a large legal apparatus governing employee benefit programs that controls when and how this can be done. This apparatus was constructed over many years as part of a developing consensus over how employer and employee needs should be balanced. There is no similar apparatus for phased retirement programs, and much of the current apparatus is in fact an impediment.

Ideally, a phased retirement program should be a routine employee benefit program that permits employees to adjust their work hours and responsibilities gradually as they transition to full retirement.[1] Its compensation and benefits—both pension and

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1. There are a number of good reports and analyses currently available on the issue of phased retirement. Among them are: *The Working Group Report*

welfare—structure should be flexible. It should provide employers with reasonable and predictable costs, minimal administrative responsibilities, and legal protection against claims for age discrimination. It should enable employees to make an informed decision about participating and maintain current law protections for older workers, particularly for those who must work out of financial necessity.

This article examines the legal issues impeding the development of phased retirement programs. The first section describes the three major laws that govern employee benefits and the features of those laws that most conflict with the objectives of phased retirement programs. It also describes how similar issues were resolved when early retirement programs were first developed on a large scale a decade ago. The next section explores the legal issues in the design of phased retirement programs from the perspective of the employer and discusses strategies that appear to be successful, although they are available only to a select group of employers. The article then reviews phased retirement programs from the perspective of the employee and describes some of their drawbacks. In the final section, a number of policy options for changing current law are considered. The article concludes with some recommendations for change—from relatively easy to accomplish regulatory changes to extensive statutory changes—that could be adopted to accelerate the development of phased retirement programs.

I. LEGAL BACKGROUND

To design a phased retirement program, an employer has to answer three basic questions. How will the work arrangement be structured? Which employees should be eligible? How will employees be paid? An employer's answer to these questions will have important legal implications. Phased retirement programs, with some limited exceptions, will fall within the category of employee benefit programs. By any standard, such programs are heavily regulated by multiple statutes and complicated regulations. The relevant statutes are designed for different purposes but a common theme—the protection of employees—is prominent in each.

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on Phased Retirement, submitted to the ERISA Advisory Council of the United States Department of Labor, Nov. 14, 2000 *available at* http://www.dol.gov/pwba/adcoun/phasedr1.htm (last visited June 8, 2002); Adrien R. LaBombarde, *Can Phased Retirement Really Work?*, Milliman & Robertson, BENEFITS PERSP. UPDATE, May 2001 *available at* http://www.milliman.com/files/PUp_0501_arl_phased.pdf (last visited June 8, 2002); and David Rajnes, *Phased Retirement: Leaving the Labor Force*, EBRI NEWSL., vol. 22, no. 9, September 2001, *available at* http://www.ebri.org/notesx/0901note.htm (last visited June 8, 2002).

This section briefly describes the major federal laws that control employee benefit plans and their pertinent features for purposes of phased retirement programs. It concludes by illustrating how a similar initiative for early retirement programs might serve as a model for legal changes to spur the implementation of phased retirement programs.

A. Special Benefits Statutes: The Tax Code and ERISA

Because they receive special tax benefits, employee benefit plans are subject to special rules in the Internal Revenue Code.[2] In addition, they are generally also subject to the federal labor law known as the Employee Retirement Income Security Act ("ERISA")[3] whose purpose is to secure the benefits promised employees in employer-sponsored plans. Nothing in ERISA or the Code requires employers to establish benefit plans or mandates the types of benefits those plans must offer. But both statutes play a critical role in structuring the plans of employers who choose to do so.

Not all plans and not all employers are subject to the full array of regulation. The plans sponsored by state and local governments and other public authorities are exempt from ERISA as well as many important Code rules and are regulated instead by state law.[4] A second exception applies to the type of plan. As a general rule, plans which pay health, life insurance or similar benefits, so called "welfare" benefits, are subject to much less regulation and scrutiny than plans that pay retirement benefits. Employers have almost complete discretion over which employees will be covered and what benefits will be offered in welfare plans. In addition, employees have no vested rights to benefits in these plans so employers are free to change these plan as they see fit. Both the Code and ERISA provide employers who include welfare benefits in their phased retirement programs with the maximum amount of flexibility.

Exhibit 1. Restrictions on Employer Flexibility

A welfare plan has few restrictions but:

- a retirement plan may impose only minimum age and service standards for participation;

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2. The Internal Revenue Code shall be referred to as either the I.R.C. or the Code within the text.

3. This act shall be abbreviated as ERISA throughout the text, and the act and its subsections shall be alternatively referred to as ERISA or Title 29 of the United States Code (29 U.S.C.) in the notes.

4. ERISA § 4(b) (2002).

- a retirement plan must cover a high proportion of low-paid workers;
- a retirement plan may not pay disproportionate benefits to high-paid workers;
- a retirement plan must have standard rules for how all participants will accrue benefits in a pension plan and receive contributions in a profit-sharing plan;
- a retirement plan's other benefits, rights and features such as loans, forms of distributions, early retirement subsidies, rights to make and receive contributions, and so on, must generally be available to all participants;
- a retirement plan must have a standard schedule for vesting; and
- a retirement plan may not reduce or eliminate vested benefits

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The opposite is true of retirement plans sponsored by private employers. Their regulatory structure reflects a philosophy that employers should be required to make their plans as uniform as possible and include a broad group of employees. As a result, employer flexibility in retirement plan design is limited. A particular plan must satisfy complicated, mathematical non-discrimination tests. Exhibit 1 illustrates some of the constraints imposed on employer discretion in retirement plan design. The rationale for these rules originates in the Code and reflects the sentiment that the tax benefits available through retirement plans should not disproportionately benefit higher-paid employees.[5] Through the passage of ERISA in 1974 and subsequent legislation, benefit law has increasingly required employers to adhere to rules promoting uniformity and standardization in the treatment of employees and types of benefits offered. As a result, as a general rule, employers find it all but impossible to create benefits specifically for special groups of workers - whether they are older workers, younger workers, or any other specific category of workers.

Technical tax rules also complicate the regulatory landscape for phased retirement programs. Here the problem is not too much uniformity but too little. Under most scenarios, these programs would anticipate relying on retirement plans to provide supplemental income to part-time retirees. But not all plans are capable of providing this income. Tax law, very early on, divided the retirement plan universe into two types: pension plans and

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5. These rules were first enacted in the Revenue Act of 1940 in an effort to ensure that a plan would cover a reasonable proportion (a "good group") of an employer's workforce and would not skew its benefits or contributions to owners, executives and other highly-paid employees. These rules have been elaborated and increasingly tightened in subsequent amendments to the Code.

profit-sharing plans.[6] Today, this distinction has lost most of its popular meaning as both types of plans provide retirement income. As a legal matter, however, the distinction is still critical, controlling important plan features such as when benefits may be paid. As a result, this distinction between plan types has a major impact on the design of phased retirement programs.

So-called pension plans are defined in regulations as those intended to pay benefits "over a period of years, usually for life, after retirement."[7] They have two basic forms: (1) defined benefit plans, including hybrid defined benefit plans such as cash balance plans; and (2) money purchase pension plans that are defined contribution plans with a set contribution formula. Profit-sharing plans are now the most common form of retirement plan.[8] Although they were originally created to enable employees to participate in the profits of their employer, employers are no longer required to have profits before making plan contributions. Profit-sharing plans have two basic forms: stock bonus plans, including employee stock ownership plans, and profit-sharing plans that include the popular 401(k) plan. Profit-sharing plans permit employers, and employees in the case of 401(k) plans, to decide each year how much, if anything, they will contribute, subject to Code limits.

Exhibit 2. Pension Plans:

- may not pay benefits before the "normal" retirement age;
- the employer decides when normal retirement age occurs;
- defined benefit plans are generally required to calculate benefits as beginning at age 65;
- age 65 used to be the normal retirement age for full Social Security benefits;
- age 65 is the customary, but not legally required, normal retirement age in pension plans;
- most pension plans cannot pay benefits to current employees before age 65;

Because pension plans are designed to pay retirement income, their ability to pay in-service benefits to employees is limited. The

6. This distinction has been in existence ever since retirement plans were first invented in the late 1800s. The latest IRS position on this issue was adopted in 1956 and can be found at Treasury Regulations § 1.401-1. 26 C.F.R. § 1.401-1 (2002).

7. 26 C.F.R. § 1.401-1 (2002).

8. Prior to the Tax Reform Act of 1986, employers could make contributions to their profit-sharing plans only in years in which they had actual profits. 26 U.S.C. § 401(a)(27)(A) (2000).

Internal Revenue Service ("IRS") has interpreted the "retirement income" restriction in pension plans to prohibit payment of benefits, other than disability and death benefits, before an employee terminates employment or the plan itself is terminated.[9] As Exhibit 2 illustrates, employers have traditionally chosen age 65 as normal retirement age, although previous studies showed that the design of defined benefit plans may actually encourage retirement before the normal retirement age.[10] Pension law does not mandate age sixty-five as normal retirement age but generally does require defined benefit plans to express benefits as an annual amount beginning, for most employees, no later than age sixty-five. Most employers choose age sixty-five as the normal retirement age in their plans in order to satisfy this rule easily and because, until recently, age sixty-five was the traditional age for retiring and receiving full Social Security benefits.

Profit-sharing plans are not prohibited from paying benefits to current employees, and employers can choose to include a number of different distribution options in their plans.[11] The technical rule is that these plans may pay benefits "after a fixed number of years, the attainment of a stated age, or upon the prior occurrence of some event such as layoff, illness, disability, retirement, death, or severance of employment."[12] Exhibit 3 illustrates the types of distribution options typically available. Tax law, however, does make a distinction between contributions made by employers and employees and imposes special limits, for example, on 401(k) contributions. A 401(k) plan may not allow current employees withdraw their own contributions prior to age fifty-nine and one-half. Younger employees may only get access to

9. Rev. Rul. 56-693, 1956-2 CB 282, *available at* http://www.taxlinks.com/rulings/1956/revrul56-693.htm (last visited June 8, 2002).

10. *See generally* Daniel Dulitzky, *Incentives for Early Retirement in Private Pension and Health Insurance Plans, in The Retirement Project, Brief No. 3*, March, 1999, Washington, DC: URB. INST., *at* http://www.urban.org/retirement/briefs/3/brief_3.html (last visited July 31, 2002); Laurence Kotlikoff & David Wise, *Employee Retirement and a Firm's Pension Plans*, in THE ECON. AGING (David Wise, ed., 1989); Laurence Kotlikoff & David Wise, *The Incentive Effects of Private Pension Plans, in* ISSUES IN PENSION ECONOMICS, (Zvi Bodie, John Shoven & David Wise, eds., 1987); Laurence Kotlikoff & David Wise, *Labor Compensation and the Structure of Private Pension Plans: Evidence for Contractual versus Spot Labor Markets, in* PENSIONS, LAB., & INDIVIDUAL CHOICE (David Wise, ed., 1985); and James Stock & David Wise, *The Pension Inducement to Retire: An Option Value Analysis in* ISSUES ECON. AGING (David Wise, ed., 1990); *See also* Rudolph G. Penner, Pamela Perun & Eugene Steuerle, *Legal and Institutional Impediments to Partial Retirement and Part-Time Work by Older Workers*, Washington, D.C.: THE URBAN INSTITUTE, 2002.

11. Each distribution option adds a layer of complexity and contributes to the record-keeping burden of plan administration that so few employers permit the maximum number of distribution events in their plans.

12. 26 C.F.R. § 1.401-1(b)(ii) (2002).

their own funds by taking a loan from the plan or by qualifying for a small "financial hardship" distribution in a limited number of circumstances.

Exhibit 3. Profit-Sharing Plans may allow current employees:

- to withdraw employer contributions after 2 years;
- to withdraw employer contributions after 5 years of plan participation;
- to withdraw employer contributions at any age;
- to withdraw contributions on account of financial hardship
- to take a loan;
- but not to withdraw 401(k) contributions (employee contributions) before age 59½.

Tax law contains an additional disincentive to early participation in a phased retirement program. Employees normally pay regular income tax when they withdraw funds from retirement plans. But current employees who take withdrawals before age fifty-nine and one-half pay an additional ten percent excise tax in addition to regular income tax, unless they lock themselves into withdrawals in the form of lifetime annuity payments.[13] Employees who quit after age fifty-five and take any form of withdrawal are not required to pay this extra tax.

This combination of plan distribution restrictions and extra tax penalties can make employees reluctant to participate in a phased retirement program with their current employer. For example, in a defined benefit plan, many employees under age sixty-five will find switching to part-time work in a phased retirement arrangement unattractive because they can not begin receiving pension payments as supplemental wages until age sixty-five. Employers could, of course, choose a lower "normal" retirement age to facilitate earlier distributions, but that would accelerate the accrual and therefore the cost, of benefits for all participants. Some have suggested, however, that liberalizing this restriction to promote phased retirement programs is warranted. The "Phased Retirement Liberalization Bill" was introduced in the last session of Congress to permit pension plans to provide in-service distributions after attainment of age fifty-nine and one-half or completion of thirty years of service. By enabling defined benefit plans to make payments to current employees before normal retirement age, such legislation would facilitate phased retirement programs.[14] In a profit-sharing plan, many employees

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13. I.R.C. § 72(t) (200).
14. The "Phased Retirement Liberalization Bill" was introduced in the

who have not reached age fifty-nine and one-half also have little incentive to stay with their current employer in a part-time work arrangement. If they quit, they not only can get complete access to their own 401(k) contributions as well as their employers' contributions, but they also avoid a ten percent penalty tax on their withdrawals if they are at least fifty-five years old.

As a result, many employees who might otherwise prefer to remain with their current employers in a phased retirement arrangement will find switching to a new employer an attractive option. If their current employer has a defined benefit plan, employees under age sixty-five who have earned or are close to earning their maximum benefits under that plan may choose to work for a new employer part-time while drawing pensions from their previous employer. If their current employer has a 401(k) plan, employees over age fifty-five may quit so they can withdraw funds without a tax penalty as needed from their 401(k) accounts rather than waiting until age fifty-nine and one-half.

Two issues are raised by the tax treatment of defined contribution plans. First, should we remove the tax penalties for withdrawals by current employees before age fifty-nine and one-half? Doing so would be more neutral with respect to the age of retirement and would rationalize the tax treatment of current and former employees. This change might also facilitate the development of more flexible partial retirement arrangements before fifty-nine and one-half. However, the tax subsidy provided for retirement savings has a clear purpose. It encourages people to provide for an adequate income for their retirement and allowing early, penalty-free withdrawals would interfere with that goal. In that sense, the philosophy of the tax law is consistent with the philosophy of compelling people to join the Social Security system. Society feels the need to protect itself against people who would otherwise irresponsibly spend too much during their working lives and throw themselves into safety net programs, such as the Supplemental Security Income program, when they are elderly.

The second question is, should pension and profit-sharing plans should be treated the same by the tax law? That is to say, both might allow penalty-free withdrawals after age fifty-nine and one-half whether or not the employee continues to work for the same employer. That would appear to be a desirable reform.

B. Special Protections for Older Workers: The ADEA

Phased retirement programs will inevitably be subject to an additional overlay of regulation under the Age Discrimination in

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House of Representatives on July 13, 2000 but was not enacted into law. 106th Cong., 146 CONG. REC. E. 1229 (2000).

Employment Act ("ADEA"). From a phased retirement perspective, the ADEA is particularly problematic. It is a highly specialized area of labor law within the family of employment discrimination statutes, and both substantively and procedurally, quite different from the tax and labor law familiar to benefits professionals. In addition, it is, however, ambiguous and not well tested when compared to its counterparts in the Code and ERISA. Its application to employee benefit plans is just beginning to be fleshed out by the courts as older employees begin to assert age discrimination claims against perceived benefit cutbacks.

Nevertheless, the ADEA will play a prominent role in the development of phased retirement programs because such plans fall squarely within its mandate of protecting older workers. It is just difficult at this time to predict the contours of its role. Court cases, rather than government statutes or regulations, typically shape the evolution of the ADEA. Because age discrimination lawsuits on benefits issues are still in their infancy, it will be many years before there is enough settled case law to measure the influence of the ADEA on employee benefit plans.

Exhibit 4. Rules Related To Age:

- employers may no longer require employees to retire;
- employers are prohibited from discriminating on the basis of age in their benefit plans;
- life insurance, health insurance, and disability benefits for older workers must satisfy an "equal benefit" or "equal cost" standard;
- a retirement plan may not refuse participation to employees on the basis of age;
- a retirement plan may not stop benefit accruals or contributions because of a participant's age;
- a retirement plan may not decrease benefit accruals because of increasing age;
- a retirement plan must vest participants at the later of age 65 or after 5 years of participation.

The ADEA forbids employers from discriminating against workers age forty and older with respect to the "compensation, terms, conditions, or privileges of employment, because of such individual's age" or "to limit, segregate, or classify . . . employees in any way which would deprive or tend to deprive any individual of employment opportunities or otherwise adversely affect his

status as an employee, because of such individual's age."[15] It applies to public and private employers with at least twenty employees. Under a recent Supreme Court case, however, state governments are immune from suits by individual employees under the ADEA.[16] Its primary influence on benefit law to date has been to eliminate rules related to chronological age that used to limit older workers' participation in benefit plans. Exhibit 4 illustrates those rules that largely apply to retirement plans.[17] The ADEA does permit a limited number of age distinctions in employee benefits plans. For example, a retirement plan may set a minimum age for early or normal retirement benefits, and defined benefit plans are permitted to pay subsidized early-retirement benefits as well as Social Security supplements.[18] In addition, employers have a defense against age discrimination claims when their actions can be justified by the terms of a bona fide employee benefit plan.[19] This defense is available, provided that the plan satisfies an "equal cost or equal benefit" standard in the benefits paid to older workers.[20] The EEOC, the agency with regulatory authority over the ADEA, however, has taken the position that the equal cost defense does not apply to retirement plans.[21]

But the full implications of this EEOC ruling are not clear, and in general, there continues to be a great deal of legal uncertainty surrounding the ADEA and its application to employee benefit plans. Section 11 of the ADEA provides that "[t]he term 'compensation, terms, conditions, or privileges of employment' encompasses all employee benefits, including such benefits provided pursuant to a bona fide employee benefit plan."[22] The ADEA does not, however, elaborate on the meaning of "a bona fide employee benefit plan." It is also silent on when a benefits plan that satisfies all Code and ERISA requirements may violate the ADEA's prohibition against age discrimination. In some instances, such as the requirement that benefit accruals continue

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15. 29 U.S.C. § 623 (2000) (corresponds to ADEA §4(a) (2002)).

16. Kimel v. Florida Bd. of Regents, 528 U. S. 62, 83-84 (2000).

17. Many of the changes made by the ADEA to benefit law are incorporated into both the Code and ERISA. Because the IRS, rather than the U.S. Dept. of Labor, typically has jurisdiction over these ADEA-related rules, they will be discussed as Code rules.

18. 29 U.S.C. §623(l)(1) (2000) (corresponds to ADEA §4(l)(1) (2002)).

19. 29 U.S.C. §623(f)(2)(B) (2000) (corresponds to ADEA §4(f)(2)(B) (2002)).

20. 29 U.S.C. §623(f)(2)(B)(i) (2000) (corresponds to ADEA §4(f)(2)(B)(i) (2002)).

21. EEOC Compliance Manual on Employee Benefits, October 3, 2000, *available at*: http://www.eeoc.gov/docs/benefits.html (last visited June 30, 2002) [hereinafter Compliance Manual].

22. ADEA §11(l) (2002); 29 U.S.C. § 630(l) (2002).

after normal retirement age, the ADEA specifically incorporates related provisions under ERISA and the Code. But the vast body of employee benefit law is not incorporated into the ADEA. In addition, the EEOC takes the position that

> [n]either [the tax code nor ERISA] is a defense to conduct that is unlawful under the ADEA . . . because neither *requires* an employer to discriminate on the basis of age. Thus the fact that a plan meets the standards of ERISA or the Internal Revenue Code is typically irrelevant in determining whether the plan is in compliance with the ADEA.[23]

Until there is more guidance on the extent to which benefit plans that satisfy the Code and ERISA must be changed to comply with the ADEA, employers will be reluctant to adopt phased retirement plans, largely because of their legal exposure. The first test of the EEOC's position should come soon in some pending litigation over the conversion of defined benefit plans to cash balance plans. Some older employees have argued that they are discriminated against by the formula used to calculate accrued benefits after a conversion. The resolution of these cases will be important not just as a matter of statutory interpretation, but because the economic stakes are high for both employees and employers. Older employees stand to lose the value of their most valuable years of benefit accruals under their defined benefit pension plans if they lose the case. If employers lose, the potential damages are very significant. In addition to paying employees the benefits they should have received as required by ERISA, an employer may, under ADEA, also be required to pay compensatory damages for mental anguish and inconvenience, as well as punitive damages for intentional discrimination, attorneys' fees and court costs.

C. A Precedent: Early Retirement Programs

One way to illustrate the legal difficulties facing phased retirement programs is to look at a precedent involving nearly identical legal issues. During the recession of the early 1990s, employers wanted to offer early retirement incentives to encourage workers to leave voluntarily through retirement rather than involuntarily through layoffs. These incentives were often structured as "windows" or short-term programs, and employers wanted to have the flexibility to decide which employees would be eligible for the program. The benefits package often included both enhanced retirement benefits and retiree health benefits.

The legal issues confronting these plans were extremely complex. Under pension law, how could a plan make a short-term program available to a select group of employees? On its face, this

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23. *See* Compliance Manual *supra* note 21, at 8.

seemed to violate long-standing pension rules promoting uniform and standard benefits and preventing employer discretion. In practice, these programs would probably violate non-discrimination rules as well because older, and presumably higher-paid, employees within the plan population could receive more generous benefits. Under the ADEA, how could an employer offer benefits that could be greater for younger workers than older workers in the targeted group? Many employers also had a practice of requiring workers accepting special early retirement offers to waive their rights to sue under various employment statutes including the ADEA. Was this permissible under the ADEA or other benefit law? Under pension law, waivers of benefits have long been subject to special scrutiny. Judges will generally only enforce waivers that can be shown to be truly knowing and voluntary.[24] Under case law, individual waivers would be either be upheld or denied, depending on the facts and circumstances of each lawsuit. As a result, because there were no uniform legal standards for waivers, employers had no advance assurance that their waivers would protect them from lawsuits.

In the end, the legal issues were so complex that resolutions came only through new legislation and regulatory action. The IRS added language to its non-discrimination regulations setting standards for special early retirement window benefits.[25]

The ADEA was amended to permit certain early retirement programs and waivers of benefits in those programs.[26] The compromise solution for early retirement programs is illustrated in Exhibit 5. In addition, the ADEA was amended to permit waivers of rights to sue provided they: 1) are part of a written agreement specifically listing the claims to be waived; 2) are effective only as to claims available before the waiver is signed; 3) include additional consideration for the employee; and 4) advise the employee to consult with an attorney, give at least forty-five days to review the offer, and provide specific information about the program including: eligibility and time limits; the job titles and ages of employees who are covered by the program; and the ages of similarly-situated employees who are ineligible. The compromise

24. *See, e.g.*, Finz v. Schlesinger, 957 F.2d 78, 82 (2d Cir. 1992) (holding that a judge must review a waiver of ERISA rights in the context of: 1) the plaintiff's educational background and business experience; 2) the amount of time the plaintiff had to review the agreement before signing it; 3) the plaintiff's role in formulating the agreement's terms; 4) the clarity of the agreement; 5) whether the employer encouraged the plaintiff to seek legal advice or whether the plaintiff was represented by or consulted with an attorney; and 6) whether the consideration given was beyond those employee benefits to which the employee was already entitled by contract or law).

25. I.R.C § 1.401(a)(4)-4(d)(3) (2002).

26. 29 U.S.C. § 623(f)(2)(B)(ii) (2000) (corresponds to ADEA § 623(f)(2)(B)(ii) (2002)).

resolution of the legal issues surrounding early retirement programs is neither elegant nor simple. It has not eliminated litigation, because there are sometimes allegations of age discrimination, but the law has generally worked in that early retirement incentive programs are now commonplace, and accepted by employers, employees, and the courts.

Exhibit 5. The Compromise Solution for Early Retirement Plans:

- an early retirement plan must be voluntary;
- an employer may set a minimum age, or years of service for eligibility;
- the plan may be offered for a limited period of time;
- the plan may be offered to selected groups of employees;
- the plan may not provide lower level benefits to older employees unless it meets the equal cost or benefits test, provides the subsidized portion of an early retirement benefit, or is a Social Security supplement plan.

D. Phased Retirement: The Employer's Perspective

Although phased retirement has become a popular topic, little data are available on the extent of these programs today. Because they are not subject to government reporting requirements, there is no systematic information about how many employers are adopting these programs. In addition, little information is available about how employers are structuring the work arrangements, deciding which employees are eligible, or creating pay policies in phased retirement plans. In the last two years, however, some exploratory studies have been conducted which provide preliminary data. The benefits consulting firm of Watson Wyatt Worldwide recently surveyed about 500 of its employer-clients on their phased retirement programs,[27] and the benefits consulting firm of William M. Mercer questioned over 200 of its clients.[28] In addition, AARP funded a number of small studies on phased retirement including a combination of interviews and case

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27. Watson Wyatt Worldwide, *Phased Retirement: A Work in Progress, 2000* , *available at*: http://www.watsonwyatt.com/search/publications.asp?Component=Insider&ArticleID=7610&nm=Watson%20Wyatt (last visited June 8, 2002); *Watson Wyatt Worldwide Phased Retirement - Reshaping the End of Work: The Business Case, 2000*, *available at*: http://www.watsonwyatt.com/search/publications.asp?Component=Insider&ArticleID=8376&nm=Watson%20Wyatt (last visited June 8, 2002) [hereinafter Watson Wyatt].

28. William M. Mercer, *Phased Retirement and the Changing Face of Retirement*, May 2001.

studies of about eighty employers.[29] Taken together, the three studies suggest the following trends:

1. Employers express interest in phased retirement, but only a small minority currently try to implement it.

Only sixteen percent of employers in the Watson Wyatt study[30] and twenty-three percent in the Mercer study[31] offered work options, programs, or plans to ease the transition to retirement. Among the sixty-five companies interviewed by AARP, about thirty percent offered part-time work or flexible schedules.[32] The studies do not reveal the typical number of hours worked nor do they describe common types of flexible arrangements offered by companies. The findings are consistent with the data from the HRS indicating that only eighteen percent of older workers are employed by firms that allow reduced hours.[33]

2. There is no uniform model for current employees.

Employers employ a variety of strategies and techniques. A common practice is to arrange part-time work for individual employees; however, a rarer practice involves formal structured programs for groups of employees.

3. Rehiring retirees for part-time and temporary work is the most common arrangement.

In addition to (or sometimes instead of) making phased retirement available to their current employees, many employers have a practice of rehiring retirees for less than full-time work from either their firm or another company. The Watson Wyatt study, for example, reported that seventy-five percent of employers with phased retirement arrangements hired retirees as part-time and temporary workers.[34] Among sixty-five companies interviewed by AARP, over sixty percent hired back retirees.[35] In the Mercer study, sixty-three percent of the surveyed employers reported have a policy of hiring retirees,[36] although it is not clear whether these were their own retirees or retirees from another company. Hiring former employees can present some difficult legal issues, discussed later in this article, for phased retirement programs.

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29. AARP, *Easing the Transition: Phased and Partial Retirement Programs: Highlights*; 1999.
30. Watson Wyatt, *supra* note 27.
31. Mercer, *supra* note 28.
32. AARP, *supra* note 29.
33. Penner, Perun & Steuerle, *supra* note 10.
34. Watson Wyatt, *supra* note 27.
35. AARP, *supra* note 29.
36. Mercer, *supra* note 28.

4. Private employers lag far behind public and not-for-profit employers in sponsoring phased retirement programs.

The Watson Wyatt study reports that employers in education, public administration, and health care offer phased retirement programs most frequently.[37]

E. Why Creating Programs for Current Employees is Difficult.

The apparent reluctance of employers to craft programs to ease the transition to retirement for current employees has many possible explanations. In the Mercer study, a large percentage of employers who reported not having a program felt that phased retirement was not a priority for them (65%) or their employees (11%).[38] Only four percent cited legal complexity as a deterrent.[39] But the numbers alone do not give a true picture. The majority of these same employers actually do offer phased retirement opportunities—just not through a plan. Their preference is to make individual retirement arrangements for selected employees, only on an ad hoc basis.

From the employer's perspective, this strategy makes a great deal of sense. It achieves the goal expressed by many employers (49% of employers in the Watson Wyatt survey[40] and 30% in the Mercer survey[41]) to retain employees with specialized skills and expertise. It provides an employer with an opportunity to be creative when deciding how the work arrangement should be structured, which employees should be eligible, and how employees will be paid. It is a perfectly legal way to avoid the hassles of a more structured program—but only up to a point. The ADEA, Code, and ERISA only regulate employee benefit "plans," so once an employer arrangement qualifies as a plan it must satisfy all the relevant rules.

Consequently, individual arrangements are a stop-gap measure at best. If an employer limits phased retirement opportunities to only a select few employees, they will work well. Even if the employer chooses only highly-paid executives, individual arrangements are permissible.[42] But if the number of employees grows and the employment arrangements are sufficiently similar, a series of individual arrangements will, at some point, become a "plan." Unfortunately, at the present time, there are no clear legal rules on when a series of informal

37. Watson Wyatt, *supra* note 27.
38. *Id.*
39. *Id.*
40. Watson Wyatt, *supra* note 27.
41. Mercer, *supra* note 28.
42. ERISA provides exemptions from its usual requirements for so-called "top hat" plans that are designed for a select group of management and highly-paid employees.

arrangements becomes a "plan."[43] Most employers will not even be aware of their potential exposure until sued by some disgruntled employee. But at that point they may encounter the full weight of liability under the Code, ERISA, and the ADEA.

When individual arrangements are no longer practical, what is the next best strategy for an employer? The survey data indicate that many employers take the first step toward a formal phased retirement program by offering reduced hours or work schedules to current employees. This type of arrangement is unlikely to be termed a plan under either ERISA or the Code because neither law regulates the work hours of employees. This is a typical practice adopted by about sixty percent of the employers in the Watson Wyatt study,[44] fifty percent of the employers in the Mercer study,[45] and thirty percent of the employers interviewed in the AARP study.[46] If this arrangement is made available to a broad-based group identified—for example, by length of service or job level—it should be reasonably free of ADEA issues. If employees merely shift to part-time work with wages and benefits correspondingly reduced, there are few legal difficulties. But merely offering part-time work would rarely be satisfactory for most employers or employees. It provides employers nothing extra to offer the employees that they wish most to retain, and it gives employees nothing more than what they could probably negotiate on their own. This also costs employees some of the welfare and pension benefits they might otherwise receive.

As a practical matter, the only feasible strategy for employers who would like to retain large numbers of employees through phased retirement is to create a broad-based formal program. Having a formal plan offers advantages to an employer. From a legal perspective, it greatly minimizes exposure to liability under state law and ADEA claims.[47] From a design perspective, however, creating a formal program can be a nightmare. As was true of

43. Although ERISA provides definitions for types of welfare and pension plans, it is often left to the courts to determine when a particular arrangement has become a plan. Courts generally consider the following factors: 1) whether there is an administrative scheme requiring employer discretion; and 2) whether there is a continuing commitment to provide benefits. *See, e.g.*, Fort Halifax Packing Co. v. Coyne, 482 US 1, 6-7 (1986) (holding that a state severance pay statute is not pre-empted by ERISA, since it does not involve an administrative scheme requiring employer discretion as would be necessary to qualify it as an "employee benefit plan" under that statute's pre-emption provision).

44. Watson Wyatt, *supra* note 27.

45. Mercer, *supra* note 28.

46. AARP, *supra* note 29.

47. If the plan is an ERISA plan, it is protected from state law claims through a preemption provision. In addition, an employer can assert a bona-fide-benefit-plan defense to claims under the ADEA.

early retirement programs before the law was restructured, employers do not have the ability under current law to create flexible, targeted phased retirement programs. Early retirement programs are much simpler from a legal perspective because they are only concerned with exiting employees. Phased retirement programs pose many more complicated issues because they are concerned with employees who are simultaneously continuing and exiting from work. Example 1 illustrates many of the legal obstacles facing an employer trying to tailor a plan to this segment of its workforce.

Example 1. Employer A wants a phased retirement program for current employees. Can it. . .

- create special increased benefits in its retirement plans just for phased retirees?
  Extremely unlikely, unless rigorous non-discrimination tax rules could be satisfied.
- limit the program just to employees in certain job categories or with designated service?
  Probably, but if only high-paid employees qualify, its retirement plans may fail tax law coverage and non-discrimination requirements.
- require phased retirees to retire fully after 5 years?
  Probably not, the ADEA prohibits a mandatory retirement.
- make distributions from a defined benefit plan to supplement pay?
  Yes, but only at the individual's option, and if he or she has reached the normal retirement age (usually age 65) in the plan.
- make distributions from a defined contribution plan to supplement pay?
  It depends. No, if the plan is a money purchase plan and the individual hasn't reached its normal retirement age - Yes, at the individual's option and if the profit-sharing plan has the usual distribution options for employer contributions - No, if the plan is a 401(k) and the individual wants to withdraw his or her own contributions before reaching age 59½ but loans and hardship distributions may be available.

- stop accruing benefits or making contributions under its retirement plans for phased retirees?
  Generally not, but there is an exception for individuals who have reached a service limit under a defined benefit plan formula.
- require phased retirees to waive participation in retirement plans?
  No.
- permit phased retirees to choose between retirement plan participation and a higher rate of current pay?
  No, this is arguably a 401(k) plan in an impermissible form.
- promise to pay phased retirees more after full retirement but not through its retirement plans?
  No, this would be a pension plan subject to, but also guaranteed to flunk, ERISA's funding, coverage and participation rules and tax code non-discrimination rules.
- promise to pay phased retirees more now?
  Yes.

As Example 1 indicates, a formal phased retirement program provides employers with little flexibility. To satisfy a combination of ADEA and tax law concerns, its eligibility criteria must be broad-based. To satisfy ERISA and tax law concerns, retirement benefits must also be broad-based and include those employees in phased retirement programs. Employers would often like to provide financial incentives to retain employees, who might otherwise retire, draw full retirement benefits, and then go to work part-time for a competitor. To be attractive, a program must offer more than part-time pay. But the most convenient sources of supplemental income, the employer's retirement plans, cannot be modified to provide a special supplement to retirement income or make other special benefits available to phased retirees. An employee may prefer additional immediate compensation to higher retirement benefits later, but an employer is not allowed to offer such a deal. Most employers must continue to fund additional benefits in their retirement plans for phased retirees.[48] While additional cash compensation is legal, this would make an employee very expensive when the additional cash is combined with a mandatory addition to retirement benefits.

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48. I.R.C. § 411(b)(1)(H) (2002).

The problems posed by retirement plans for phased retirement arrangements are not entirely due to current laws that promote uniformity and standardization of participation and benefits, although they do play a significant role. Neither are the tax rules that control the timing of distributions that much to blame. These rules all create disincentives for employers to sponsor and employees to participate in phased retirement programs, but they do not absolutely prevent it. More fundamental and intractable disincentives can be found in the structure of retirement plans themselves, with defined benefit plans being the primary culprits.

Employers have long found defined benefit plans useful as a tool to promote retirement at a predictable age, usually no later than age sixty-five and often much earlier. Defined benefit plans are not age-neutral. Participants typically accrue benefits under a formula that maximizes benefits around normal retirement age for a full-career employee. The Code does impose certain accrual standards known as "anti-backloading" rules to make sure participants accrue a reasonable portion of their benefits earlier in their careers. But, as a practical matter, employees often receive their most valuable benefit accruals earlier than the normal retirement age. Previous studies demonstrated that once past the age at which benefits accrue most rapidly in typical private-defined benefit plans, further accruals provide little, if any, incentive to work longer.[49]

Moreover, the majority of plans contain early retirement options that provide a substantial incentive for retirement before normal retirement age. These permit employees to retire at an earlier-than-normal retirement age, usually age fifty-five to sixty-two, after completing fewer—generally between fifteen and twenty years of service—than the number of years required for a full retirement benefit. Early retirement benefits are attractive because they are frequently subsidized by the use of favorable actuarial calculations.

Defined benefit plans have these characteristics because for decades employers found them useful devices for rationalizing the retirement process for their workforces. Now that later retirement is an issue, they have a perverse effect because their accrual structure cannot be easily adapted to encourage later retirement. Employers are generally not free to amend their plans to remove or cutback on early retirement subsidies because these are protected benefits under the Code's non-discrimination rules.

It is also difficult for them to terminate their defined benefit plans and replace them with other plans. Defined benefit plans are expensive to terminate because tax law imposes a fifty percent

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49. Penner, Perun & Steuerle, *supra* note 10.

excise tax on excess assets returned to the employer after all benefits have been paid. Converting them into defined contribution plans is not an option either because this just results in de facto plan termination. The only feasible option for employers is to convert their plans into "cash balance" plans that are defined benefit plans with defined contribution features. Participants accrue benefits under these plans through a more age-neutral, front-loaded formula, and few provide early retirement subsidies. But even this option is not easy.

Not all employers will want to make the substantial changes a conversion requires, such as developing a new plan formula and funding schedule, re-drafting the plan document, informing participants, and obtaining the IRS's approval. In addition, cash balance plans have achieved certain notoriety among employees. Older employees, for example, find that the benefits they accrue under the cash balance design are far less than they would have accrued under the defined benefit plan. In addition, many employers add a "wear away" feature to their plans as part of a conversion. This usually means that older employees actually receive reduced or no contributions to their cash balance accounts for several years until the value of any early retirement subsidies accrued under the defined benefit plan has been eroded. Employees have argued that such features constitute age discrimination, and these issues are currently in litigation. Many employers have responded to the controversy over cash balance conversions by adding some additional protections for older workers. Some let employees choose between the new cash balance formula and the old defined benefit formula. Others grandfather more of the benefit previously subsidized in the defined benefit plan. If this trend continues, cash balance conversions will become even more common among employers and more acceptable to employees.

Defined contribution plans, because they are legitimately age-neutral and more front-loaded, do not provide incentives for early retirement that are as powerful as those provided by defined benefit plans. Participants receive contributions based on their annual compensation as long as they continue to work. In some circumstances, defined contribution plans can even contain incentives for continued work. Depending on the demographics of an employer's workforce, defined contribution plans can have an age-weighted allocation formula so that older workers receive higher employer contributions than younger workers. Over the past ten years, defined contribution plans have become the dominant form of retirement plan. Employers who offer only defined contribution plans—and this is now the majority of employers among those with retirement plans—find phased retirement programs easier to implement, even under the

limitations of current law.

F. Why Hiring Retirees is Preferred

Many employers have found (or believe they have found) a satisfactory alternative to the difficulties presented by formal programs for current employees. They hire retirees—their own and retirees of other companies. Some sixty percent of employers in the Mercer study,[50] as well as those interviewed in the AARP study,[51] reported a policy of rehiring retirees.

There are a number of popular arrangements. Many hire retirees for part-time and temporary work. For example, seventy-five percent of employers in the Watson Wyatt study[52] and sixty-three percent of employers in the Mercer study[53] who rehire retirees offer this option, and an additional 15% of employers maintain a pool of retirees for temporary work. Some 24% of employers in the Mercer study[54] will even rehire retirees full-time. Hiring retirees as consultants - without benefits - is also common. Over 60% of the employers who hire retirees in the Mercer study[55] and over 40% of the employers in the Watson Wyatt study[56] will use consulting arrangements.

On its face, hiring retirees seems an obvious solution to the problems associated with current retirees. It gives employers an opportunity to attract workers with specialized skills and expertise, usually on a flexible, as needed basis. It also appears to provide employers with the ability to negotiate employment arrangements that provide flexibility in determining compensation and benefits costs. All in all, a win-win situation—but generally only if the retirees are from some other company. For many employers, hiring former employees is hardly trouble-free. The type of arrangement—whether the retiree is hired as an employee or a consultant—largely determines the scope of the difficulties.

When their former company hires retirees as employees, the problematic issue is the employer's benefit plans. Again, defined benefit plans are the primary culprits. Defined benefit plans may not pay benefits before termination of employment or attainment of normal retirement age. Many employers adopt a popular strategy to satisfy this rule—the "retire/rehire" scenario. In this case, employees who would like to begin receiving retirement benefits while continuing to work resign or retire but are soon rehired—sometimes the next day—by their former employer. The

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50. Mercer, *supra* note 28.
51. AARP, *supra* note 29.
52. Watson Wyatt, *supra* note 27.
53. Mercer, *supra* note 28.
54. *Id.*
55. *Id.*
56. Watson Wyatt, *supra* note 27.

law is very clear that employees must truly terminate employment to be entitled to retirement benefits from pension plans before normal retirement age. But the law is unclear about what constitutes a termination of employment that satisfies the rule.[57]

So many employers take advantage of the absence of clear guidelines and bestow retiree status liberally. There is little risk of detection and even less risk of enforcement. Few employees would sue because the arrangement only benefits them, and federal regulators would only become aware of the issue—if even then—through a detailed plan audit. On the other hand, the penalty for being caught—possible plan disqualification and loss of tax benefits for all plan participants—is severe. Many employers are more cautious and require a waiting period before former employees are rehired. In the Mercer study, employers who rehire their own retirees reported requiring a mean waiting period of 5.2 months.[58] Although this is a judgment call, most pension experts would agree that this waiting period would probably satisfy the rule, provided that it was not part of a clearly prearranged agreement.

The retire/rehire problem, of course, only applies to an employer's former employees. All retirees hired as employees, however, may pose problems for an employer's benefit plans. Many employers would like to restrict participation by retirees. This is relatively easy to do in welfare plans if employers are careful either to define the category of eligible employees to exclude retirees, where possible, or to keep their hours worked below the minimum required, generally twenty hours a week, for participation. A thousand-hour a year threshold for participation applies in most retirement plans but is generally effective only with respect to "new" retiree employees.

Although employers are allowed to exclude employees in the above categories from retirement plans and other benefits, most former employees are eligible to resume participation in their employer's plans immediately upon rehire.[59] Including retirees

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57. There is little IRS guidance on this point. Its most complete explanation can be found in a relatively obscure document, General Counsel Memorandum, 38924 (July 26, 1990). This document discusses the legal difference between the terms "severance from employment" for purposes of making pension distributions, and "separation from the service", a term used to define a lump sum for purposes of obtaining favorable tax treatment for a distribution.

58. Mercer, *supra* note 28.

59. Although an employer may exclude certain categories of employees from retirement plans, the IRS looks with disfavor on any excluded category called "part-time employee" or "temporary employee." It takes the position that these definitions could violate ERISA's minimum service standards for participation. As a result, most employers are not able to exclude retirees from their retirement plans by defining them as part-time. Retirees can be

who work part-time in plans is not only an expense for employers, it is often an administrative burden if the retirees work only sporadically or infrequently. Employers usually still must track the hours of service performed by these retirees to determine whether they are eligible for an additional benefit accrual or a contribution each year.

Many employers prefer to avoid the benefits eligibility issue for retirees entirely by hiring them through consulting contracts. A consultant is an independent contractor, not an employee, and is therefore ineligible for employee benefits programs. This solution works well from a legal perspective provided that the retiree actually is an independent contractor. The difference between an independent contractor and an employee from a legal perspective is a judgment call. However, a very important test under IRS regulations is whether the individual sets the conditions—how, when, and where—of his or her work.[60] There are no statistics on this point, but it is very likely that many retirees, called independent contractors, cannot satisfy this standard. They typically perform the same job as consultants that they performed as employees, looking and acting more like employees than not.

Until recently, misclassification of employees—designating employees as independent contractors to avoid paying benefits—was not a major legal issue. Now it is a hot topic because individuals who were classified as independent contractors have brought several high-profile class action lawsuits seeking retroactive employee status to obtain benefits. The IRS and the Department of Labor have initiated enforcement actions against several large employers to obtain benefits wrongly denied and FICA taxes owed to employees misclassified as independent contractors.[61] Hiring retirees as consultants is still an appropriate strategy for the careful employer, but the penalty of worker misclassification—from past FICA payments to retroactive plan benefits—is high and more certain than in the past.

G. Why Public Employers Have an Advantage

Since the early 1980s, public sector employers, such as public colleges, universities, and offices of state government, have been developing phased retirement programs with innovative benefits features. These employers have long been aware of the problems posed by an aging workforce because their employees tended to be

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excluded only if they fall into some bona fide employee classification excluded from the plan, or fail to satisfy a length of service requirement.

60. *See* Rev. Rul. 1987-1 CB 296 (describing the IRS issuance of a list of twenty factors that are used to determine whether an individual is an employee or independent contractor).

61. Viczaino v. Microsoft, 120 F.3d 1006 (9th Cir. 1997) (en banc) is the leading case in this area.

long service employees. State and local governments provide a wide range of benefits to their employees on a uniform basis. Many of those benefits—such as healthcare—continue for retirees. So state and local governments already have in place many of the components of a phased retirement program that private employers typically do not. But state and local governments shared one disadvantage with the private sector - the disincentives to continued employment contained in their defined benefit plans. Taking advantage of their exemption as public employers from ERISA, and many of the more complicated tax rules governing benefit plans, they developed a plan, typically called a "Deferred Retirement Option Plan" ("DROP"), that adds pension incentives to their phased retirement programs.

Example 2. A Typical DROP

Employees enter a phased retirement program. They set a future retirement date. While they continue to work part-time:

> benefit accruals cease under the defined benefit plan;
>
> benefit payments begin but are held in separate defined contribution account in the plan;
>
> these amounts earn interest and often a cost-of-living adjustment.

At full retirement, employees receive:

> *the balance in their accounts in a lump sum, as well as annuity payments, usually for life, from the defined benefit plan.*

A DROP is a defined benefit plan that has a special defined contribution feature for employees who work past normal retirement age. Example 2 describes the characteristic features of a DROP. Usually, employees cease accruing benefits under the defined benefit plan on a specified date when their benefit is frozen. While they continue to work, the pension they would otherwise have received (if they had retired) is credited to a special account in the plan and earns interest either at an amount stated in the plan or based on the interest earned by the plan as a whole. Many DROPs require an employer contribution to the account as well. In some DROPs, mandatory employee contributions, if required, are also made to the DROP account. When the employees actually retire, they begin receiving annuity payments calculated on the basis of their frozen benefit under the defined

benefit plan. They are also entitled to receive their DROP account payable in a lump sum, installments, used to purchase a larger annuity.

A DROP offers the following advantages to employees. It provides them an opportunity to earn additional pension credits in the form of interest after they may have maxed-out under the standard defined benefit plan formula. Even if they have not maxed out, the interest credited to their DROP account may be greater than the amount of any additional accrual they would have otherwise received. It also provides employees with a large lump sum payment—rarely available under a standard defined benefit plan—upon actual retirement. At the same time, they continue to be guaranteed their lifetime monthly income from the defined benefit plan. One drawback of a DROP is that it does not provide any pension income while the employee continues to work. So this type of phased retirement program is only likely to appeal to employees who can afford to work part-time because they have other resources.

The advantages to employers are both financial and administrative. DROPs provide employers with more control over increases in benefit accruals and therefore the financial requirements of their plans. Depending on the particular plan, however, cost savings are not guaranteed and plan expenses may in fact increase. Many DROPs also require employees to agree to retire within a stated number of years, usually five, as a condition of entry. So employers also have more information about their future personnel needs while retaining the services of experienced employees for a transitional period. This does not necessarily mean that employers have some discretion over participation in the DROP. Unlike their private sector counterparts, most public sector plans cover large groups of employees with few exclusions. Participation in a DROP is typically available to all employees who meet uniform eligibility standards so employers are not guaranteed to retain only the employees they prefer.

The legality of DROPs is not entirely free from doubt. Individual plans may raise questions over whether the DROP accounts satisfy contribution limits or other defined contribution plan rules or whether the DROP accounts comply with the requirement that defined benefit plans provide definitely determinable benefits. There are also some concerns about whether the required retirement provision violates rules against mandatory retirement, despite the voluntary nature of DROPs. But DROPs have functioned successfully throughout the public sector for some twenty years, and they are unlikely to be subject to serious legal challenge at this point.

Tax law and ERISA have a number of provisions that prevent private sector employers from creating DROPs. For example,

DROPs are usually unable to satisfy rules on coverage and discrimination because they are not usually made available to a broad group of employees. In addition, the IRS's interpretations of current law make DROPs financially unattractive to some employers. Internal Revenue Code § 414(k) permits a defined benefit plan to contain separate accounts that are treated as a defined contribution plan.[62] But while the law provides this mechanism for implementing DROPs, recent IRS interpretations have made it difficult for private sector employees to do so. The IRS has taken the position that excess assets in defined benefit plans may not be used to fund 414(k) accounts without being treated as a reversion of plan assets to the employer.[63] This means that an employer would have to fund these accounts with new contributions or pay income tax and a 50% excise tax on plan assets used for that purpose. As a practical matter, DROPs are not currently available to private sector employers as a component of a phased retirement program.

H. Phased Retirement: The Employee's Perspective

Employees are attracted to phased retirement programs for several reasons. For many older workers, longer employment is a necessity because they are not financially prepared for retirement. For others, the financial rewards of work are less important than the personal satisfaction that work can bring. Some value the social interactions of work and the importance of opportunities to maintain relationships with friends and colleagues. Still others enjoy exercising the expertise and skills that they have developed over their work lives. For these workers, leaving the workforce entirely is neither desirable nor practical. Phased retirement programs can therefore fulfill a variety of needs—both economic and psychological—for these workers while adding flexibility and a better balance between work and family to their lives.

Even if not motivated by monetary considerations, employees who enter a phased retirement arrangement need to pay close attention to its economics. These arrangements have financial as well as lifestyle implications. Benefit laws, and therefore benefit plans, are full of legal quirks and pitfalls for the unwary employee. In addition, phased retirement programs have no formal disclosure requirements. For many workers, a phased retirement program may neither be a good idea, nor a beneficial deal.

I. Protecting Pension Expectations

For most employees, the most important consideration is whether a phased retirement arrangement will adversely affect

62. I.R.C. § 401(k) (2002).
63. Priv. Ltr. Rul. 9723033 (Mar. 10, 1997).

the retirement benefits that they will eventually receive. In many respects, the law has built-in protections for older workers. Older workers continue to participate in their employer's retirement plan and receive additional accruals or contributions. Rehired former employees are generally immediately re-admitted to those plans. But employees, particularly those in defined benefit plans, should be aware of the following issues.

First, employees who participate in "final average pay" defined benefit plans should not switch to part-time work before reaching normal retirement age. These plans use a formula that largely bases benefits on the average salary earned in the years closest to retirement. Employees who switch to part-time work as they near retirement age lose valuable benefits because their ultimate retirement benefits are calculated on a much lower average salary. The IRS has recently indicated that such reductions may be questionable.[64] But without a firm IRS position on this point, employers will not change this common practice.

Second, many employees rely on benefits from a defined benefit plan to supplement income from part-time work. But many plans, at the employer's option, stop benefit payments to employees who continue to work past normal retirement age or are rehired after payments have begun.[65] In the Mercer study, 51% of employers with defined benefit plans reported stopping benefit payments to employees working after normal retirement age while nineteen percent did not.[66] It is not clear from the study whether employers are formally "suspending" benefits or merely postponing payments until actual retirement, with adjustments for delayed payment. These issues are extremely technical, and it is difficult to estimate their importance to most phased retirees. It is likely that they will be significant only for those employees whose

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64. In 2000, Richard Wickersham, a senior IRS representative, stated to an American Bar Association subcommittee meeting that the IRS took the position that a final average pay plan may not reduce the already accrued benefit of an employee whose compensation decreases because this would violate the rule against an accrued benefit's decreasing on account of continued service. Under this position, a phased retiree in a final average pay plan shifting to part-time work would not be at risk for losing already accrued pension benefits. But this position is not well-publicized or enforced, and, as a practical matter, many employees in this situation do receive reduced benefits. For an excellent discussion of this issue, as well as suggested alternatives, see Patricia L. Scahill & Jonathan Barry Forman, *Protecting Participants and Beneficiaries in a Phased Retirement World*, a paper presented at the SOC'Y ACTUARIES CONF. ON DEMOGRAPHIC & FAM. CHANGE, June 25-26, 2002, San Francisco, California, *available at*: http://www.soa.org/library/monographs/retirement_systems/m-rs02-2/m-rs02-2_tableofcontents.html (last visited July 30, 2002).

65. 29 U.S.C. § 1053(a)(3)(B) (2000)(corresponding to ERISA § 203(a)(3)(B) (2002)).

66. Mercer, *supra* note 28.

motivation to enter into a phased retirement arrangement is primarily financial. These are the individuals, of course, who most need to protect and enhance their future pension expectations as they continue to work. But these laws are so complicated—as are the plans themselves—that it is unlikely that participants will be able to appreciate the difficulty of the choices before them without individual counseling.

J. The Drawbacks of Part-Time Work

For older workers, pension benefits are perhaps their most valuable employee benefit. Other benefits such as health insurance are also important and, in some cases, critical. Older workers not yet eligible for Medicare cannot obtain or afford medical insurance on an individual basis. Although some may have coverage through a spouse's health plan or from a former employer through either COBRA or a retiree health plan, an employer-sponsored plan will be vital for many.

Employees in phased retirement programs typically receive fewer fringe benefits than full-time employees as illustrated in Example 3. In the Mercer study, thirty-five percent of responding employers reported offering no health benefits to older workers on part-time work schedules, thirty-five percent offered the same benefits at the same cost, twenty percent offered the same benefits but at a higher cost, and ten percent offered different benefits.[67] In the Watson Wyatt study, nearly one hundred percent of employers provided health care, life insurance, and paid vacation benefits to their full-time employees, but only eighty percent, seventy-one percent and forty-seven percent, respectively, did so to their phased retirees.[68] Nearly all employers provided disability coverage for full-time employees but less than forty percent did so for phased retirees. Many employers who do provide benefits reduce them for phased retirees. Watson Wyatt reported that sixty-six percent provided reduced life insurance, forty percent reduced paid vacation, thirty-two percent reduced disability, and twenty-nine percent reduced health care benefits.[69]

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67. *Id.*
68. Watson Wyatt, *supra* note 27.
69. *Id.*

Example 3. Other Benefits Issues of Phased Retirees

Compared to other employees, phased retirees may receive:

- no health insurance, more costly health insurance, or different health insurance;
- less or no life insurance benefits;
- less or no disability insurance benefits;
- less paid vacation time.

It is not clear from these studies whether these employers created formal benefits policies for phased retirees or merely treated them as they do other part-time employees. It is well known that part-time employees fare poorly from a benefits perspective. Pension law has the strongest protection for part-time benefits, requiring employers in most cases to cover employees who work at least 1,000 hours a year. But employers are generally free to set any eligibility criteria they like for other fringe benefits. Those criteria often set at least a half-time standard for participation and exclude various categories of employees such as part-time or temporary workers. Neither the Code nor ERISA set explicit coverage or non-discrimination standards for most welfare benefits. The ADEA does provide that employers must provide fringe benefits without regard to an employee's age and establishes an "equal cost or equal benefit" standard for health, life, and disability insurance. But that standard only applies with respect to the benefits provided older versus younger workers. It does not set a standard for part-time versus full-time employees.[70]

II. AN ACADEMIC MODEL OF PHASED RETIREMENT

Higher education institutions have been leaders in developing phased retirement programs. These are special purpose programs designed for faculty members who have life-tenure. When the ADEA eliminated mandatory retirement in 1987, it temporarily provided an exemption for tenured faculty members at academic

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70. From a pension perspective, employees who work part-time every week are treated the same as those who work full-time many weeks, but take extra vacation time. The general standard is that employers must count, for pension purposes, individuals who work at least 1,000 hours a year. An employee's work pattern while earning those hours is usually not relevant.

institutions. Prohibitions against mandatory retirement for faculty did not become effective until 1994; until that time, mandatory retirement at age seventy continued to be permissible. When that exemption expired, the academic community became concerned that many faculty would wish to continue working past age seventy. If this occurred, it would hamper their ability to hire new faculty and increase their personnel costs. At the same time, many institutions were concerned about the loss of large numbers of faculty that would soon be reaching retirement age. The higher education community became interested in formulating a more orderly transition to retirement for its faculty. At the same time, it felt constrained by legal uncertainties about the scope of the ADEA (and its early retirement exception) and therefore was unwilling to create programs without some protection against age discrimination claims.

The result was the Higher Education Amendments of 1998 to the ADEA, which created a safe harbor for age-based faculty retirement incentive programs.[71] The safe harbor permits additional voluntary benefits to be paid, even though based on age, as a retirement incentive, provided that 1) the employer is an institution of higher education; 2) only employees with unlimited tenure are eligible; 3) the benefits are payable upon voluntary retirement; 4) no other age-based reductions or elimination of benefits occurs; 5) the supplemental benefits are in addition to pre-existing retirement or severance benefits; and 6) eligible faculty have 180 days to elect to participate.

A recent study by the American Association of University Professors of some 1,400 public and private colleges and universities indicates that the ADEA safe harbor has been extended to phased retirement programs which enable a faculty member to transition into retirement over a number of years rather than all at once.[72] These help faculty transition into retirement through part-time work as well as by continuing part-time work after formal retirement. About a quarter of the private institutions in the study reported having phased retirement programs, representing 50% of doctoral degree granting, 33% of master degree and 31% of baccalaureate degree private institutions.[73] Parallel figures for public institutions are 31%, 23%,

71. This exemption is found in ADEA § 4(m) (2002). *See also* David L. Raish, *Age-Based Retirement Incentives for Tenured Faculty Members: Satisfying the Legal Requirements*, *in* TO RETIRE OR NOT? RETIREMENT POLICY AND PRACTICE IN HIGHER EDUCATION, ch. 3 (2001). (offering a fuller explanation of the exemption).

72. Ronald G. Ehrenberg & Michael J. Rizzo, *Faculty Retirement Policies after the End of Mandatory Retirement*, (TIAA-CREF Institute, Research Dialogue #69, Oct. 2001).

73. *Id.*

and 24%, respectively.[74]

Faculty phased retirement programs have a number of innovative features as described in Example 4. Unlike their counterparts among both private and public employers, they provide *enhanced* benefits for phased retirement, rather than just a pro-rata portion of a standard benefits package or the reduced benefits offered to all part-time employees. In other respects, these programs are similar to those available elsewhere. Some seventy-five percent establish a minimum age for eligibility with age fifty-five being most common, and some twenty-five percent also establish a maximum age, usually between sixty-five and seventy. Another seventy-five percent require minimum years of service—between ten and twenty years—for eligibility. Many plans require participants to agree to relinquish tenure and agree to retire fully at specified dates. Some 16% of programs permit faculty to work part-time and retain tenure as long as they wish. But most limit the amount of time tenured faculty can participate in their phased retirement program with three to five years being a common period.

Example 4. Phased Retirement Programs for Faculty

The faculty member works part-time but may receive:

- defined contribution plan contributions based on a full-time salary
- a full year's accrual under a defined benefit plan
- enhanced pay (60% pay for 50% work)
- full employer contributions for health plan premiums.

Institutions with defined contribution plans are twice as likely to offer phased retirement programs as institutions with defined benefit plans. In part, this reflects the difficulties that even these institutions have with providing incentives for continued work through defined benefit plans. But it probably also reflects the fact that many private institutions of higher education offer only defined contribution plans. The Code permits these institutions to offer a special type of defined contribution plan that is not subject to the same complicated coverage, participation and non-discrimination rules as corporate plans.[75] As a result, academic employers have much more flexibility to tailor

74. *Id.*
75. I.R.C. § 403(b) (2002).

the benefits in these plans to select groups of employees, even those that are highly-compensated, and apparently many have done so successfully.

Academic phased retirement programs are therefore quite different from those available in the corporate world. For example, they are the only phased retirement model explicitly authorized by law, even though they are just, legally speaking, a special case of "early" retirement programs. In exchange for this legal certainty, academic employers are required to provide enhanced benefits to phased retirees. No specific benefits are mandated; employers have the freedom to design their own programs. Employees are required to receive full disclosure about the program's features and time to decide whether to participate. Although employers might wish for more tax law flexibility in designing the retirement benefit component of their phased retirement programs, the model now in place has many features the corporate employer might find attractive. All in all, it seems to provide a careful balancing of the needs of both employers and employees. As a result, phased retirement programs, at least for faculty, are becoming an accepted employee benefits program in the academic community.

III. SOME POLICY RECOMMENDATIONS

In the introduction, the following objectives for phased retirement programs were listed: 1) a flexible compensation and benefits (both pension and welfare) structure; 2) reasonable and predictable costs, minimal administrative responsibilities, and legal protection against claims for age discrimination for the employer; 3) full disclosure and informed consent for the employee; and 4) maintenance of current law protections for older workers, particularly for those who must work out of financial necessity. Achieving all these objectives in the current legal climate is not feasible. Benefit laws are complicated and rigid, and they are designed to serve objectives that often conflict with the needs of phased retirement programs. Even piecemeal reform will be difficult until there is a consensus on the appropriate scope of these programs and the legal changes required to implement them. There are no simple and easy reforms available that would bring immediate, meaningful progress in the development of phased retirement programs.

The following recommendations therefore take an incremental approach. First, this section discusses some reforms that could be achieved relatively easily through additional regulatory guidance. Next, it describes some relatively non-controversial statutory changes that have a reasonable chance of passage. More systematic and comprehensive reforms are then considered, using existing early retirement programs as a

reference point. Finally, some long-term benefits issues that affect both older and younger workers and require more fundamental reform of ERISA are briefly addressed.

A. Regulatory Guidance

Regulatory guidance is an obvious starting point for reform. This requires no real changes in law or new legislation. It only requires regulatory authorities to provide more information on their position regarding a particular legal issue. In terms of phased retirement programs, more substantive guidance on the following issues would be invaluable:

1. When does a bona fide termination of employment occur?

This is a critical issue for phased retirement programs because it determines when distributions can be made from pension plans. The "facts and circumstances" approach taken by the IRS on this issue is not helpful and has led to widespread disregard of the law. Until employers have some clear guidelines, compliance with this basic benefits rule will be low because there is no real risk of enforcement action. The IRS could provide some guidance by issuing guidelines describing a number of safe harbor scenarios or by discussing more fully the factors employers should consider. This would provide some reassurance and reinforcement for the careful employer while reining in some of the more abusive practices such as the retire/rehire charade or bogus consulting agreements that are common today.

2. How is final average pay calculated for part-time employees?

The IRS needs to clarify this issue. Phased retirement programs are not attractive to employees in defined benefit plans whose benefits are based in part on their salary averaged over the years closest to retirement. Switching to part-time employment close to normal retirement age will have adverse consequences for their ultimate retirement benefits. The IRS has recently suggested that it is impermissible to reduce an employee's already accrued benefits in a final average pay plan when compensation decreases. This issue has significance far beyond phased retirement programs. Most benefits practitioners and employers are not aware of this position, and reducing benefits is a common practice. So if this is the IRS's position, it is critical that the IRS discloses and publicizes the legal basis for this position. It is hard to overemphasize the importance of additional guidance from the IRS on this issue, because it not only affects the qualified status of most final average pay plans, but also the retirement income of millions of participants as well.

B. Statutory Changes

A number of statutory changes have recently been suggested to remove some of the perceived obstacles, largely in tax law, to the development of phased retirement programs. These are relatively non-controversial but their implications for pension policy over the long-term have really not been explored. Some of the alternatives are to:

1. Permit distributions from pension plans before normal retirement age.

The Phased Retirement Liberalization Bill introduced into Congress last year would repeal the current restriction on distributions in defined benefit plans that are in effect for those who elect to terminate employment before the normal qualifying retirement age.[76] In its place, a new rule would permit employees to begin distributions without terminating employment after they reach the earliest of normal retirement age, age fifty-nine and one-half or thirty years of service.[77] This would remove one of the major obstacles to phased retirement programs now present in defined benefit plans. But the bill also raises a number of important concerns because adding a distribution option to a defined benefit plan has financial implications for both employers and employees. Would it apply to only current employees or to terminated, vested participants too? What reduction factors would apply to these benefits and could they be subsidized? What effect would they have on early retirement benefits? Would it apply to money purchase pension plans as well? Is it good pension policy to increase the outflow of benefits before normal retirement age? The private pension system already has a problem with "leakage," that is, with retirement benefits being consumed before actual retirement.[78] This bill addresses one of the fundamental problems facing phased retirement programs and it also raises a number of important issues that should be studied further.

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76. *See supra* note 14.

77. *Id.*

78. There is considerable evidence that many employees who withdraw funds from their employers' retirement plans spend them rather than roll them over into an IRA. *See, e.g.*, Leonard Burman, Norma Coe & William Gale, *What Happens When You Show Them the Money: Lump Sum Distributions, Retirement Income Security and Public Policy,* (Urban Institute Nov. 1999); Paul Yakoboski, *Retirement Plans, Personal Saving and Saving Adequacy*, EBRI Issue Brief, No. 219, Mar. 2000; James Poterba, Stephen Venti & David Wise, *Pre-Retirement Cashouts and Foregone Retirement Savings: Implications for 401(k) Asset Accumulation* (NBER Working Paper, W7314, Aug. 1999).

2. Permit distributions from 401(k) plans before age fifty-nine and one-half.

It is a tax law anomaly that employees in profit-sharing plans can routinely obtain distributions of their employers' contributions but must wait until age fifty-nine and one-half to access their own. This rule prevents many younger employees from participating in phased retirement programs if they intend to rely on their own savings to supplement their income for part-time work. The rationale for this rule is not quite clear, but it presumably is intended to reduce leakage and to ensure that the tax advantages available under 401(k) plans flow only to long-term savings. Should such goals be imbedded in tax law? To some degree, the restrictions reflect the paternalistic worry that people will spend irresponsibly without them. Their removal would encourage earlier transitions from full-time employment to part-time employment and complete retirement. The focus of this paper is on providing more employment flexibility at later ages and therefore, removing the restrictions at this time is not a high priority. This might be reconsidered at a later date, however, especially if there is an explicit decision to reduce the tax burden on income more generally and to increase it on consumption by treating all saving more generously.

3. Liberalize pension distributions after normal retirement age.

Under current law, employers control the timing of payments from pension plans. Even if employees work after normal retirement age, they may not be entitled to receive benefits until they actually retire. In some cases where plans apply the suspension of benefits rules, employees lose benefits if they continue to work while in other cases employees receive adjusted benefits, but only at full retirement. A good argument can be made that after normal-retirement-age employees who continue to work should have the same access to their benefits as retirees. Implementing such a change requires repealing the suspension of benefits rules, changing rules on the timing of payments, and requiring fair actuarial adjustments for all delayed payments. These changes will increase plan costs for employers. On the other hand, giving employees the option to choose when their benefits begin, and ensuring that they are not penalized financially for continued work, seem like reasonable steps toward making work after normal retirement age more attractive.

4. Provide employees with more benefits information near retirement age.

Employers are now required to give employees a great deal of information about their benefits. However, that information does not necessarily help an employee trying to decide whether to retire

or to continue to work. It makes sense to require employers to provide more information that is both personalized and targeted to the retirement decision. For example, it would be helpful to employees if they were told each year how much additional accrual they would receive from their defined benefit plans for an additional year of work. In addition, employees entering phased retirement arrangements should receive full disclosure on the benefits they are foregoing, as well as receiving, from continued work. Requiring such disclosure does not impose a large administrative or financial burden on an employer because, in most cases, the necessary information is already routinely available.

5. Rationalize the penalty tax regime.

The Code imposes a ten percent penalty tax, in addition to regular income tax, on distributions made before an employee reaches age fifty-nine and one-half.[79] Exceptions in the rule shield distributions made in the form of annuities, the most common form of distribution from a defined benefit plan.[80] Lump sum and installment distributions, the typical forms of distribution from a defined contribution plan, are fully subject to the tax.[81] This rule has two rationales: to discourage leakage and to raise revenue. In terms of phased retirement programs, it represents another disincentive to participation for younger workers who intend to rely on their defined contribution plans for supplemental income. The issue is identical to that raised by restrictions on 401(k) distributions. Although the focus of this paper is not on younger workers, it seems reasonable to retain the penalty tax regime for now.

C. A More Comprehensive Proposal

The regulatory changes proposed above and the ability to receive pensions before the normal retirement age will make phased retirement programs marginally easier for both employers and employees. It is hard to escape the conclusion, however, that explicit statutory authority for phased retirement programs will be required before they can become a routine employee benefit. The age discrimination issues are too difficult and pension law is too rigid, complex, and counterproductive for any easy solutions. In many ways, the difficulties confronting phased retirement programs are very similar to those facing early retirement programs a decade ago. To resolve those issues, all three major benefit laws—the Code, ERISA, and ADEA—were amended to

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79. I.R.C. §72(t)(2)(A)(i) (2002).
80. I.R.C. §72(t)(2)(A)(iv) (2002).
81. I.R.C. §72(t)(1) (2002).

make early retirement programs feasible.[82] The same could be done for phased retirement programs even though their legal issues are in many respects more difficult. The initial step would be to:

1. Create a statute authorizing phased retirement programs.

Using the present ADEA early retirement statute as a model and taking into account the innovative plan designs now found in DROP plans and faculty retirement incentive plans, a phased retirement program statute would have the following central features. It would:

- provide legal protection to employers against ADEA claims;
- ensure the continued qualified status of retirement plans;
- set standards if certain benefits are required to be provided, if any, as well as for any benefit reductions;
- minimize the administrative responsibility of the employer;
- provide disclosure and informed consent standards for employees;
- permit employers to offer short-term plans;
- provide employers with more flexibility on eligibility, both in terms of age and income.

2. Permit safe harbor benefits and plans.

In addition to providing employers with general legal principles for creating phased retirement programs, the statute could also authorize specific safe harbor benefits and plan designs. Safe harbors provide employers with certainty that their plan designs satisfy all legal requirements. This is an important consideration in benefit law where legal standards are generally extremely inflexible. For example, adding late retirement provisions to a defined benefit plan is currently both legally risky and prohibitively expensive for employers. But a safe harbor authorizing separate benefit accrual standards just for phased retirees might be very attractive to employers. Safe harbors could also benefit special retirement plans just for phased retirees. In addition, the statute could define a safe harbor basic benefits package that, if made available to phased retirees, would permit employers to exclude them when testing their plans for non-discrimination under Code rules. A phased retirement statute with safe harbors represents an opportunity to restore some flexibility to benefit law, provided it authorizes and encourages employers to experiment with innovative benefits packages while safeguarding the interests of employees. Such a statute, for example, could:

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82. 29 U.S.C. § 623(f)(2)(B)(ii) (2000); I.R.C § 1.401(a)(4)-4(d)(3) (2002)

- provide safe harbors that lessen regulatory restrictions to permit more innovative plan designs such as DROP plans;
- permit special plans and benefits packages just for phased retirees;
- add late retirement features to defined benefit plans;
- define a basic benefits package that permits complying plans to exclude phased retirees from tax law non-discrimination tests;
- exclude phased retirees from non-discrimination testing under 401(k) plans.

One drawback to using the current statutes as models is that each requires employers to provide additional consideration, such as enhanced benefits to participants. Employers seem to accept this requirement when it benefits highly-favored employees such as faculty or reduces their other costs through employment terminations. Employers, however, may not be willing to do this for large numbers of employees who are continuing to be paid while accruing additional benefits. As a result, a phased retirement statute may require a different incentive structure if it is to appeal to employers. On the other hand, many employers might believe that retaining or obtaining experienced, valued employees is worth the price of some additional, not necessarily lavish, fringe benefits, provided they have some flexibility in designing a benefits package that fits their own needs as well as those of phased retirees.

D. A Longer-Term Issue

From an employee's perspective, many of the disincentives in phased retirement programs have nothing to do with age, and have everything to do with part-time work. Part-time workers receive proportionately fewer (if any) benefits—both welfare and pension—than their full-time co-workers. Phased retirees frequently find that by reducing their hours they lose a disproportionate share of their fringe benefits. This practice has long been sanctioned by ERISA. ERISA, however, was enacted over twenty-five years ago when the model employment pattern was the nine-to-five job and long-term service with a single employer.

Perhaps phased retirement programs can serve as a vanguard for revisiting the treatment of part-time work under ERISA. With respect to pension plans, ERISA has an "all or nothing" standard. In general, employees who work at least 1,000 hours a year are entitled to be eligible for pension benefits. Employees who work less may be and are generally excluded from their employer's pension plans. Their only alternative for accumulating retirement

income is to make their own contributions to an IRA. ERISA fails to provide even a minimum-hours standard for health and other fringe benefits. Although many employers do provide these benefits routinely, they also often exclude part-time workers from their health, disability, and life insurance benefit programs as well. This leaves part-time workers in the position of having to purchase often-costly individual benefit policies, if they can even afford such benefits, because they are not permitted access to the less expensive group insurance market.

IV. CONCLUSION

The labor market has changed a great deal since ERISA was passed. New work arrangements such as "flex-time", "telecommuting", or "just-in-time worker" hiring policies are bringing valuable flexibility to the workforce and the workplace. But ERISA is incapable of facilitating the benefits issues posed by such creative work arrangements because its fundamental statutory framework is static, inflexible, and uncreative. Phased retirement programs raise many of the same issues that flexible work policies must confront. Similarly, these programs provide a test case for developing a new consensus between employers and employees over the appropriate treatment of less than full-time work. By working through the benefits issues for phased retirees, the development of phased retirement programs—whether through a special statute or by adding flexibility to existing law—should help to modify ERISA to meet the needs of the twenty-first century workplace.