Statement of Randy G. DeFrehn
Executive Director
National Coordinating Committee for Multiemployer Plans
Washington, DC

Before the Subcommittee on Employer-Employee Relations
U. S. House of Representatives

"Reforming and Strengthening Defined Benefit Plans: Examining the Health of the Multiemployer Pension System"

March 18, 2004

Mr. Chairman and members of the Committee, thank you for this opportunity to meet with you and discuss one of the most important domestic policy issues facing our nation: the long-term financial viability of the defined benefit pension system and specifically, the multiemployer defined benefit pension system. I represent the National Coordinating Committee for Multiemployer Plans. As you might expect with a name like that, it will come as no surprise that we are known more simply by our initials: the NCCMP.

I. Background

The NCCMP is a non-partisan membership organization comprised of multiemployer plans and their sponsoring employee and employer organizations. It is the only national organization devoted exclusively to protecting the interests of the plans and the approximately ten million workers, retirees, and their families who rely on multiemployer plans for retirement, health and other benefits. Our purpose is to assure an environment in which multiemployer plans can continue their vital role in providing benefits to working men and women. The NCCMP is a nonprofit organization, with members, plans and plan sponsors in every major segment of the economy, including, among others, those in the building and construction, retail food, trucking, service, textile, health care, communications, printing, steel, mining and entertainment industries.

We commend the Subcommittee on its work in this matter as well as the Committee on Education and the Workforce. In his opening statement upon convening the current Conference considering HR 3108, Education and the Workforce Chairman Boehner stated that his overriding goal "…is simple: to protect the pension benefits of American workers." We find that goal to be commendable and completely consistent with the objectives of the NCCMP and the multiemployer funds we serve.

II. Multiemployer Plans: Often Misunderstood

Multiemployer plans have been a major force in the delivery of employee benefits to active and retired American workers and their dependents for over half a century. Although they are often mistakenly referred to as "Union" plans, these plans have operated under a statutory mandate since the passage of the Labor – Management Relations Act of 1947 (also known as the "Taft-Hartley Act"), under a structure that requires equal representation by labor and management in the operation and management of the funds. Furthermore, the fiduciaries who control the assets of the benefit plans are obligated under the Act to manage the plans for the sole and exclusive benefit of the fund participants. While this statutory requirement provides sufficient incentive for plan trustees (most of whom serve without compensation) to take these responsibilities seriously, ERISA's fiduciary responsibility provisions place their personal assets at risk in the event they violate these obligations.

For industries characterized by large numbers of small to medium sized employers and / or a mobile workforce, the multiemployer structure is the only way that many employers are able to offer competitive health and pension benefits to their employees, by enabling them to take advantage of the economies of scale and shared administrative costs. It is estimated that approximately 60,000 to 70,000 employers contribute to multiemployer plans and that upwards of 90% of such contributing employers are small to medium sized businesses, employing fewer than 100 employees. Similarly, the portability features of multiemployer plans enable employees in such industries to carry credited service in defined benefit pension and other benefit plans with them as they move among contributing employers within a given industry. While by definition, a multiemployer plan requires contributions pursuant to a written agreement between at least one union and more than one employer, union membership is *not* a condition of participation, eligibility, or receipt of benefits from multiemployer plans.

Operationally, contributions to multiemployer plans are usually a function of the hours worked by covered participants, although other structures permit contributions on other bases such as weekly, monthly or by some other measure of productivity.[1] The amount of such contributions is determined by the bargaining parties or "settlors" through the collective bargaining process and is fixed for the term of the bargaining agreement (usually three, but five year terms are not unusual). There is an explicit trade-off between wages and benefits, as the funds from which contributions are made would otherwise be part of the wage package. Based on assets available and on the advice of plan professionals, including the enrolled actuary, the plan trustees then determine the level of benefits to be provided. It is important to note that in most situations (especially those involving national plans), the individuals who bargain the contribution levels (usually at the local level) are not the same as those who serve as trustees. A national plan could receive contributions pursuant to literally hundreds of distinct, local bargaining agreements.

Benefits provided under these plans are not typically related to salary, but are based on a unit value. This could be expressed as a flat dollar per month per year of service or by a percentage of contributions. Depending on the industry and the plan, the value of past service may or may not be increased over time. Unlike most single-employer plans, but consistent with their statutory obligation to administer these plans for the sole and exclusive benefit of plan participants, the majority of multiemployer plans provide periodic increases for retired participants.

Under the current funding rules, plan fiduciaries must ensure that the required contributions are collected as owed and in a timely manner. To facilitate this process, most have well defined collection procedures, including procedures to collect interest, collection fees and liquidated damages, from delinquent employers. These contributions are held in trust for the payment of

[1] Early plans in the mining industry called for contributions per ton of coal produced.

benefits, reasonable administrative costs and to fund future benefits when they are due. As these are generally mature plans, over time the contributions held for future benefits have evolved into the primary source of income for the trust. They are managed by qualified professional asset managers (know as QPAMs under ERISA) who are also plan fiduciaries. Under asset diversification policies encouraged by the Department of Labor, trust assets have been held in a broad variety of asset classes, including equities and fixed income, real estate and more recently and to a much lesser extent, other types of asset categories (hedge funds, international funds, venture capital). Multiemployer plans are typically more conservative than their single-employer counterparts with equity allocations generally averaging 50% to 55%. These allocations are established by the trustees in consultation with their professional advisors, including investment consultants, investment advisors and managers and actuaries.

By design, multiemployer plans feature an interrelationship among contributing employers that is not found in the single-employer community, causing them to be inherently more stable. Because of the mobility and portability features, employers fund a portion of an employee's benefit with the remainder paid by other contributing employers for whom that individual may have worked during his career. Because they are contributing to a pooled benefit plan for a pool of employees, the departure or demise of a given member of the pool has certain consequences, both for the departing employer and for those who remain. Although the rules governing those consequences vary by industry, the general rules require that if an employer ceases to participate (either voluntarily, through bankruptcy, or retirement) in a fund that has no unfunded vested benefits, there are no consequences for that employer or the other employers and the employees can move on to a different contributing employer to continue to accrue additional vesting and benefit credits. If an employer voluntarily ceases to participate in a fund that has unfunded vested benefits it is assessed its proportionate share of those unfunded vested benefits, based on a formula that tracks its contributions over a period prior to its departure. This is a requirement that was added in the Multiemployer Pension Plan Amendments Act of 1980 (MPPAA) and is known as "withdrawal liability[2]." The trustees would file a claim, and then proceed to collect the amounts due in a manner similar to its delinquent contribution procedures.

If the withdrawing employer has insufficient assets to pay its withdrawal liability, or if that liability is capped under certain provisions of MPPAA, the remaining liability is left with the remaining contributing employers, to be funded over time similar to an investment loss. While there are certain notable exceptions, withdrawal liability has proven over time to be an additional motivating factor to the parties to ensure that the plans' funding levels are sufficient to fully fund the present value of vested benefits. Although there are withdrawal liability methods utilized by some plans that more directly attribute an employer's withdrawal liability to that employer's contributions (with interest) offset by benefit payments and accrued liabilities of his own workforce, for the most part the pooled methods have been little more than a footnote for the vast majority of plans during most of the last 25 years. This has changed recently and mainly as a direct result of the three consecutive years of negative performance in the equity markets, unprecedented since the decades before the adoption of ERISA's funding rules in 1974.

[2] Before the enactment of the withdrawal liability provisions of MPPAA, a withdrawing employer could abandon its accumulated liabilities and effectively shift the responsibility for funding them to the remaining employers, many of whom were their competitors. The competitive edge to be gained by doing so actually provided an incentive to employers to do so.

The concept of interconnectedness of contributing employers is an important element in understanding how they differ from single-employer plans and why these plans have posed an insignificant risk to the Pension Benefit Guaranty Corporation (PBGC) since the multiemployer fund was initiated in 1980. According to PBGC, there were 1661 multiemployer defined benefit pension plans in 2002, down from 2,244 in 1980, while at the same time the number of participants grew from approximately 8 million in 1980 to slightly more than 9.5 million in 2002. Much of the contraction in the number of plans was related to significant merger activity during the 1990s. Almost none of the plans became the wards of the PBGC, with only 31 plans ever having received any financial assistance since the creation of the multiemployer guaranty fund in 1980. This is contrasted with the single-employer guaranty fund which has taken over approximately 3,100 such plans through the end of 2002.[3]

More than any other testament, this record speaks well for the long-term structure of this private sector system as it is currently constituted.

III. Historically and Still Well Funded

In addition to commenting on the Committee on Education and the Workforce's objective to protect the benefits of the American worker, Chairman Boehner made the observation that "the multi-employer pension system is basically sound and financially healthy." We concur with that conclusion. In fact, according to a recently issued survey, the average funded position of multiemployer pension plans in 2003 (based on plan years that ended in 2002) was 87%[4]. While that represented a decline from 95% in 2002, it still reflects a favorable funded position looking to the funds' ability to meet their long and short- term benefit payment obligations. By industry, the funded positions ranged from a high of 91% for retail trade and food, to a low of 85% for transportation. According to the latest PBGC data the funding ratio for multiemployer plans was 104% as of 2000. The average funding ratio of PBGC insured plans for the 20 year period from 1980 through 2000 dropped below 90% only one year (1996 when it was 88%). For eight of those years the ratio exceeded 100% with the remainder ranging from 91% in 1999 to 98% in 1992 and 1993[5].

Although the latest PBGC annual report showed a deficit in the multiemployer fund for the first time in 20 years, when one looks behind the conclusion it is clear that the primary reason for this shift is related to the historically low long-term interest rates used in determining the funding levels. We are confident that the plans covered by the multiemployer guaranty fund present no substantial long-term risk to the PBGC or, more importantly, to the participants of those plans and when the rates return to more normal levels the perceived deficit will disappear.

Part of the reason why multiemployer plans have traditionally been so well funded is that the contributions to the funds are negotiated and mandated in a collective bargaining or other agreement that requires contributions to the plan, regardless of the performance of the investment

---

[3] See PBGC Data Trends 2002

[4] See the Survey of the Funded Positions of Multiemployer Plans 2003 issued by The Segal Company, an international actuarial and benefits consulting firm.

[5] See PBGC Data Trends 2002

markets. Unlike single-employer plan sponsors which tend to fund defined benefit plans at the minimum funding requirement (a policy that resulted in the absence of any contributions for a number of years to such plans when the investment markets significantly outperformed the assumed rates of return), multiemployer plan sponsors continued to make contractually mandated contributions throughout that period. Since they also benefited from the bull markets in the 1990s, however, multiemployer plans encountered a different type of problem -- the full funding limitations.

It is estimated that upwards of 75% of all multiemployer defined benefit plans encountered funding limitations during the 1990s that would have resulted in the employers' inability to take tax deductions for contributions to these trusts and accompanying excise taxes. Because the plan trustees were generally not the same parties as the settlors who set contribution rates in the collective bargaining agreements, the trustees were forced to increase benefits to protect the deductibility of the employer contributions. This prevented the funds from accumulating a contingency reserve to offset the unanticipated steep and prolonged declines in the investment markets such as those encountered from 2000 through and including 2002. Although this problem was partially addressed legislatively in 2001, a permanent exclusion to the maximum deductible limits for multiemployer plans seems indicated in any comprehensive reform measure.

IV. Principles of Reform

The preceding background describes a system that has largely evolved into a well conceived, self-correcting system in which private sector employers and employee representatives have negotiated contributions that have been wisely invested to provide secure retirement income to tens of millions of plan participants.

In evaluating the issues that might be the subject of a reform initiative, we would do well to borrow a line from Hippocrates who, in reference to disease is reported as having said "…make a habit of two things – to help, or at least, do no harm." The following recommendations for guidelines to observe when considering any reform proposal are offered in that vein.

First, multiemployer plans are fundamentally different from single-employer plans. Therefore, solutions for single-employer plans cannot be applied to multiemployer plans without thought, study and adaptation to multiemployer situations. For example, funding tests that are based on employers' individual business hardship are not reasonably adaptable to multiemployer plans, because, among other things, each employer's financial information must be kept confidential vis-á-vis the other contributing employers (including the employer trustees) who are competitors, and the union.

A second tenet is that the funding requirements must be level and predictable, so that the trustees can set benefit levels with some confidence that the fund's probable investment and contribution income will be able to meet the statutory standards. This includes rejecting any proposal that would cause the fund to be subject to greater volatility, such as the elimination or reduction in the ability of a plan to use sound actuarial smoothing methods. The recent experience with our unprecedented declines in U. S. equity markets, compounded by historically low fixed income rates presents the best case for not making sweeping policy changes at either extreme lows or extreme highs.

A third point to consider is that multiemployer funding requirements must be adaptable to the realities of the collective bargaining process from which the contributions arise. This underscores the need for level, predictable funding requirements, including the need to phase-in funding increases to avoid sudden demands for dramatic contribution increases that could disrupt the bargaining process. An essential element of this concept is an assurance that the bargaining parties will have an opportunity to address new funding demands in bargaining so that neither the employers nor the participants are penalized because contribution levels cannot be changed during the term of the collective bargaining agreement.

Forth, given the wide variety of circumstances and issues affecting bargaining, trustees and the bargaining parties need flexibility to meet the funding standards using whatever approaches best match the economics of their industry. Therefore, the law should specify the funding goal, but give the parties and trustees substantial leeway in setting the path to reach it. Furthermore, the funding rules should allow for benefit designs that participants will regard as fair: to retirees, to those nearing retirement, and to the population of active employees who generate the contributions.

Fifth, the multiemployer funding regime should aim for benefit security and participant satisfaction – not “PBGC protection” or “100% funding at all costs.” Such a concept is somewhat perverse – that the very agency that was established to provide a safety net for plan participants would contribute to funding policies that would discourage employers from continuing them. Full funding, as a goal, and for setting funding targets for PBGC purposes, should be measured on a going-concern rather than termination basis for plans that are in fact going concerns.

Sixth, the funding and tax rules should not inhibit responsible funding through the imposition of deduction limits and penalties that make it impossible for plans to build up strong reserves in the good years as a buffer against future bad years. It should also be noted that “bad years” in the context of multiemployer plans include periods in which there is little work for the active participants that generate the contributions, as well as those in which there are investment market reverses.

Seventh, funding rules need to respect intergenerational equity – do not ask for too much sacrifice from current actives or retirees during a funding crisis, but ask enough from each generation of actives so that its costs are not knowingly being passed on to the next group.

Eighth, do not force multiemployer plans, even mature multiemployer plans, into a uniform investment mode in order to minimize financial risk. Recognize that defined benefit plans inherently incorporate a balance between promised benefits and the risk that the plan’s assets could fall short, regardless of how sizeable the funding reserves appear to be at any given point. A defined benefit plan remains alive only to the extent its assets (invested and contributed) can grow to meet the growing benefit needs and expectations of its participants. Striving for full funding, on a mark-to-market basis, at any time would not only be futile, it could also end the defined benefit plan's ability to serve its participants as they expect and deserve**.**

Finally, withdrawal liability is almost universally disliked within the multiemployer world by employers and unions alike, but some hedge is needed to prevent strong employers from abandoning plans and leaving liabilities to roll over onto the weaker employers or to the guarantee system. Even in declining industries, the withdrawal liability system has worked to protect the participants without shifting obligations to the PBGC.

V. Conclusion

In the earlier joint hearing held with the Committee on Education and the Workforce, you heard a number of experts comment on the administrative and regulatory compliance complexities that accompany the sponsorship of defined benefit plans. Multiemployer plans suffer from many of the same problems and concerns and we urge you to continue your work to eliminate such obstacles to the long term health and survival of these plans.

As we look forward to the coming decades in which the baby-boomers retire and the coming generations face an uncertain future, wondering how they will cope with the costs of Social Security and Medicare, all the while being convinced that neither of these programs will be there for them, we would do an even greater disservice to them by failing to salvage the defined benefit system that has provided those who have gone before us - our fathers and mothers - with a dignified retirement. The continued decline of the defined benefit system in favor of the empty promises of a defined contribution retirement system that too few low to moderate income workers can afford to utilize and those who do vastly underestimate the amount they will need in their lifetime, will only serve to foist ever more of a financial burden on those future generations. As future retirees outlive their money, the costs of their care, even at a subsistence level, will be shifted to the taxpayer.

If the volatile market performance of the past three years has taught us nothing else, we should have learned that only a defined benefit pension will keep us from returning to the days of the County poor house to house our indigent elderly.

As the Committee proceeds with its work to strengthen the defined benefit system, we hope that you will consider ways that some of the features of the multiemployer system, such as portability of service, could be adapted to the single-employer system to encourage greater participation in defined benefit plans. We are eager to assist the Committee in its work in any way you choose to do so.

Thank you very much. I welcome any questions you may have.