**TESTIMONY OF THE
NATIONAL COORDINATING COMMITTEE FOR MULTIEMPLOYER PLANS
BEFORE THE
COMMITTEE ON WAYS AND MEANS
SUBCOMMITTEE ON OVERSIGHT
ON PENSION ISSUES**

May 5, 1998

The National Coordinating Committee for Multiemployer Plans ("NCCMP") submits these comments in support of H.R. 3632, which would eliminate the rules in Section 415 of the Internal Revenue Code that are forcing reductions in the benefits of workers covered by multiemployer pension plans.

The NCCMP is the only national organization devoted exclusively to protecting the interests of the more than nine million workers, retirees, and their families who rely on multiemployer plans for retirement, health and other benefits. The NCCMP's purpose is to assure an environment in which multiemployer plans can continue their vital role in providing benefits to working men and women. The more than 240 Affiliate and Associate Affiliate members of the NCCMP encompass plans and plan sponsors in every major segment of the multiemployer plan universe. The NCCMP is a nonprofit organization.

To understand why multiemployer plans and their participants need the relief provided in H.R. 3632, it is important for you to understand the basic characteristics of these plans. Therefore, these comments first describe the unique characteristics of multiemployer plans and then describe the need for relief from the Code section 415 limitations.

I. CHARACTERISTICS OF MULTIEMPLOYER PLANS

Multiemployer plans are common in industries characterized by many small employers and highly volatile employment patterns, such as the construction trades, garment, trucking, longshore, entertainment, etc. Often participants in these plans will work for only a brief period for any one contributing employer, and work for numerous employers each year.

Multiemployer plans add up these periods of service for eligibility, vesting and benefit accruals. They provide two elements for their participants and contributing employers that all observers agree are sorely needed in the pension system generally to make it feasible for small employers to provide pensions -- full portability for mobile workers and efficiencies and economies of scale in plan administration.

Multiemployer plans are funded based on contribution rates fixed in collective bargaining agreements that typically run for a period of at least three years. These agreements require employers to contribute a set dollar amount per hour worked, or other measure of service or unit of production, for each employee covered by the bargaining agreement. The total contributions to the plan therefore fluctuate based on increases and decreases in covered work in the industry.

Employee representatives typically negotiate a dollar per hour labor cost with employers. The hourly dollar amount of current wages is generally this total labor cost, reduced by the amount of plan contributions. Thus, as a practical matter, employees are making benefits contributions out of their current hourly wages.

Multiemployer pension plans typically provide either flat dollar benefits or benefits equal to a dollar amount times years of service. Unlike the standard for single-employer plans, multiemployer plan benefit formulas are rarely based on a participant's compensation.

Favorable investment experience over the past decade, plus the parties' commitment to maintain steady funding for pension, has allowed many plans to increase benefits in recent years. These increases have usually taken the form of higher normal retirement benefit levels. In addition, some plans have reduced the amount of covered service needed during a year to earn a benefit credit.

II. THE NEED FOR MULTIEMPLOYER PLAN RELIEF FROM PROVISIONS OF TAX CODE SECTION 415

Largely because of these unique characteristics, multiemployer plans need relief from certain provisions that were never intended to have the effect they have on such plans.

A. Exemption from Code section 415 100 Percent of Compensation Limit

H.R. 3632 provides a much needed multiemployer plan exemption from the provision of Code section 415 that limits the benefits that can be paid under a pension plan to 100 percent of the participant's average compensation for the three consecutive calendar years in which it was the highest.

The Code section 415 limits are designed to prevent highly compensated individuals from using pension plans as tax avoidance schemes to defer excessive pension benefits. This does not happen in the context of multiemployer plans.

However, due to the unusual structure of multiemployer plans, the work patterns of their participants and the manner in which the contribution streams that fund them are negotiated, they face a risk of running afoul of the 100 percent of compensation limit. Where this happens, the participants who are hurt by the limit are the lowest paid rank and file workers covered under the plan -- the exact opposite of the type of participants these rules were designed to impact.

As discussed above, multiemployer plans typically provide the same annual retirement benefit to a participant or to all participants who have the same number of years of service. It is extremely rare for a multiemployer plan benefit formula to be based on compensation. Multiemployer plan benefit formulas are therefore very advantageous to lower paid workers. As a percentage of compensation, the more money a participant makes the smaller is his benefit. The effect of these formulas is to provide an adequate retirement benefit even to the lowest paid of these workers, by, in effect, subsidizing such benefit by providing relatively lower benefits to the higher paid workers.

Ironically, it is this very antidiscriminatory aspect of multiemployer plans that creates much of their problem under the 100 percent of compensation limit. The level of plan benefits is set by the trustees with one eye towards what the contribution stream funding the plan can support and the other eye towards the reasonable retirement needs and expectations of the average plan participant. This benefit may, however, be higher than the 100 percent of compensation limit for plan participants who were paid significantly less than the norm.

Another problem is created by the work patterns of many multiemployer plan participants. In a typical single employer plan, a plan participant is employed continuously with the same employer during his period of participation in the plan. Over time, due to inflation, that participant's compensation will increase. Because this employment is continuous, the three consecutive years in which compensation is the highest -- that is, the three years on the basis of which the 100 percent of compensation limit is computed -- will typically be the last three years. Thus, in effect, single employer plan participants get the benefit of cost of living adjustments to their 100 percent limit while they are working, because they get the full advantage of their compensation increases due to their continuous employment. Once they leave service, their 100 percent limit is also directly adjusted annually under section 415(d) to reflect increases in the cost of living.

In the context of multiemployer plans, the 100 percent of compensation limit sometimes shrinks, despite cost of living increases in pay rates. As multiemployer plan participants grow older, they may find it more difficult to secure continuous employment. The gaps between their periods of employment may become more frequent and more prolonged. This is especially true in industries characterized by hard, physical work, especially outdoors, or work in extreme climates. Even though the hourly rate may reflect inflation, a reduced number of hours worked during some portion of any period of three consecutive years may prevent that period from being used as the base for computing the 100 percent limit. If an earlier group of three years is used, the worker is deprived of the automatic inflation adjustment to this limit that the typical single employer plan participant would obtain through a salary increase. In addition, because the participant has not yet retired, no direct inflation adjustment to the limit is allowed. This shrinking of the limit is particularly pronounced in declining industries where work has become more scarce in general.

Plan trustees recognize that multiemployer pension benefits have, in effect, been paid for by the plan participants. In some declining industries, to prevent participants from losing their benefits due to inability to find continuous employment, trustees have reduced the number of hours per year necessary to earn a pension credit. For some participants this can increase the severity of the impact of the 100 percent of compensation limit, as their actual pay may decline -- even if hourly wage rates go up -- because they are working fewer hours. Although it looks as though they are earning additional pension benefits, these participants hit the 100 percent limit and lose their pension benefits anyway.

It is important to note that it is not possible to adjust plan contributions to deal with this problem. Multiemployer plan contribution rates are set through collective bargaining. The rate set for any particular collective bargaining unit is uniform, typically because the hourly wage package is uniform. There is no practical way to provide different contribution rates for different workers depending on the number of hours they work, even if it were possible to know or to predict the number of hours a particular worker would work during a particular year. Contributions can only be reduced across the board, and if they are, wages or other benefit plan contributions would need to be increased across the board to maintain the equilibrium and follow through on the bargained-for compensation. So the majority would be denied an adequate pension to avoid having the pension of the lowest-paid among them exceed the 415 limits.

Ironically, the 100 percent of compensation limit is not a problem for highly compensated employees generally. Employers maintaining single employer plans typically provide benefits in excess of the Code section 415 limits for highly compensated employees through unfunded excess benefit plans. This is not a feasible solution in the context of multiemployer plans. The Taft-Hartley Act requires multiemployer plan benefits to be provided through a trust.

To understand the harshness of the impact of the 100 percent limit on plan participants, it is important to note that, from the worker's perspective, this limit is imposed retroactively. Plan participants ordinarily compute their benefits using the formulas they find in the summary plan descriptions and with reference to their years of service. They make plans for retirement based on the benefits so computed. They usually do not realize the amount of reduction in their benefit that will be made due to the 100 percent limit until they actually retire and make a claim for benefits.

We therefore urge you to exempt multiemployer plans from the 100 percent of compensation limit.

B. Exemption from Code section 415 Reductions in Pension Benefits on Early Retirement

H.R. 3632 would provide for multiemployer plans the same section 415 dollar limit for early retirement benefits that applies to tax-exempt entity and government employees.

Code section 415(d) imposes a dollar limit on the annual benefit that may be paid from a defined benefit plan. This dollar limit is $90,000, indexed for inflation. This amount is far higher than the typical multiemployer plan benefit and is ordinarily not a problem for multiemployer plans.

However, the dollar amount is reduced actuarially for benefits that start earlier than normal retirement age. This actuarial reduction can have a severe impact on early retirement benefits.

Many multiemployer plans provide pensions that can be taken on an unreduced basis after a certain number of years of service, e.g., 30. These are referred to, for example, as "30 and out pensions" or "service pensions." In industries that involve hard, physical labor, it is often not feasible for participants to work past their early or mid-50s. For someone who has been working at these backbreaking jobs since high school, "early" retirement represents a well-earned chance to stop working so hard. These special service pensions are reasonably designed to address the income needs of such workers. Yet the section 415 dollar limit could restrict such workers to receiving little more than $40,000 or so a year.

To prevent this dollar limitation from becoming so low that it interferes with the ability of multiemployer plans to provide adequate retirement benefits to early retirees, H.R. 3632 would allow multiemployer plans to use the same rule that is currently available to plans maintained by government and tax exempt organizations. This rule is found in Code section 415(b)(F) and is the rule that was in place before the Tax Reform Act of 1986. Under this rule, the dollar limit will be reduced only below age 62 and will not be reduced below a dollar amount that is the actuarial equivalent of a $75,000, indexed, limitation at age 55.

*****

We appreciate this opportunity to provide testimony on H.R. 3632 and the need for relief for multiemployer plan participants from the Code section 415 rules. We would be pleased to provide additional information at the Committee's request.