Testimony of
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Mr. Chairman and Members of the Committee:

I am pleased to be here today to discuss the subject of reforming multiemployer defined benefit pension plans. I appear here on behalf of a broad coalition of plans, employers, employer associations and labor organizations that sponsor multiemployer plans which has put forth a carefully negotiated, balanced proposal for multiemployer pension plan reform. The coalition proposal has evolved through the efforts of many of the system's largest stakeholders since the Pension Funding Equity Act of 2004 failed to provide meaningful relief to even a single multiemployer plan, despite the laudable efforts of a majority of the Members of this Chamber. A list of those groups who are participants in the coalition is enclosed with my written remarks, but it is important to note that they represent the overwhelming majority of employers and virtually all of the unions in the construction, trucking, entertainment, service and food industries and the membership of the National Coordinating Committee for Multiemployer Plans (NCCMP) which directly represents over 600 jointly managed pension, health, training and other trust funds and their sponsoring organizations across the economy. The NCCMP is a non-profit, non-partisan advocacy organization formed in 1974 to protect the interests of plans and their participants following the passage of ERISA and the increasingly complex legislative and regulatory environment that has evolved since then.

Background

There are nearly 1600 multiemployer defined benefit pension plans in the country today. They provide benefits to active and retired workers and their dependents and survivors in virtually every area of the economy. Because of their attractive portability features, multiemployer plans are most prevalent in industries, like construction, which are characterized by mobile workforces. According to the latest information from the Pension Benefit Guaranty Corporation, multiemployer plans cover approximately 9.7 million participants, or about one in every four Americans who still have the protection of a guaranteed income provided by a defined benefit plan. With few exceptions, these are mature plans that were created through the collective bargaining process 50 to 60 years ago and have provided secure retirement income to many times that number of participants since their inception. Although some mistakenly refer to them as "union plans" the law has required that these plans be jointly managed with equal representation by labor and management on their governing boards since the passage of the Labor Management Relations (Taft-Hartley) Act in 1947. This active participation by both management and labor representatives (most of whom are participants in the plans) provides a clear distinction between single employer and multiemployer plans. They are more extensively regulated under both labor and employee benefits laws and regulations and the watchful eyes of the Department of Labor, the Internal Revenue Service and the Pension Benefit Guaranty Corporation. Most important among these laws and regulations, Taft Hartley requires that the fiduciaries who serve on these joint boards must manage these plans for the "sole and exclusive benefit" of plan participants, and ERISA imposes fiduciary obligations on plan fiduciaries that put at risk the personal assets of those who fail to meet their obligations.

It is estimated that there are over 65,000 employers that contribute to multiemployer plans. The vast majority of which are small employers. For example, in the construction industry, which makes up more than 50% of all multiemployer plans (but just over one-third of the participants), it is estimated that as many as 90% of all such employers employ fewer than 20 employees. By sponsoring these industry plans, employers are able to ensure that their employees have access to comprehensive health and pension benefits and, through the jointly managed training and apprenticeship plans, the employers have access to a readily available pool of highly skilled labor, none of which could be feasible for individual employers to provide.

Funding for multiemployer plans comes from the negotiated wage package agreed to in the collective bargaining process. For example, if the parties agree to an increase in the wage package of $1.00 per hour over three years, the $1.00 may be allocated as 40¢ to the health benefit plan, 20¢ to pensions, 5¢ to the training fund and the remaining 35¢ taken in increased wages. Although for tax purposes, contributions to employee benefit plans are considered to be employer contributions, the funding comes from monies that would otherwise be paid to the employee in the form of wages. For the overwhelming majority of such employers, their regular involvement with the plans is limited to remitting their monthly payments to the trust funds as required pursuant to their collective bargaining agreements. For most contributing employers, these funds are the perfect substitute for a large financial commitment to human resources functions, providing administrative services and meeting today's complex compliance requirements while providing economies of scale that would otherwise make such benefit plans unaffordable for small business.

Since the passage of the Multiemployer Pension Plans Amendments Act of 1980, participants of multiemployer plans have been covered by the benefit guarantee provisions of the PBGC. Unlike single employer plans, however, the PBGC is the insurer of last resort for multiemployer plans. Instead, the employers who contribute to these plans self-insure against the risk of failure of another. Under the multiemployer rules, employers who no longer contribute, or cease to have an obligation to contribute to the plan, must pay their proportionate share of any unfunded vested benefits that exist at the time of their departure. This obligation, known as withdrawal liability, recognizes the shared obligations of employers in maintaining an industry-wide skilled labor pool in which employees may move among contributing employers dozens of times during their career. This system of shared risk has protected both the participants and the PBGC, as evidenced by the fact that it has had to intervene in fewer than 35 cases over the past 25 years. The reduced risk to the PBGC is also reflected in a much lower premium - $2.60 per participant per year, versus $19 per participant per year plus a variable premium for single employer plans. The PBGC guarantees a much lower benefit for multiemployer plans - a maximum of $12,700 per year for a participant who retires at normal retirement age after 30 years of service (adjusted proportionally for greater or less service),compared with a maximum benefit under the single employer guarantee of approximately $44,000 annually. As of the latest PBGC annual report, the multiemployer guaranty program showed a projected deficit of approximately 1% of that projected for the single employer guaranty fund.

This system of pooled risk has been both one of the greatest strengths and major weaknesses of the multiemployer system. In the early 1980s, the presence, or even the threat of withdrawal liability produced a chilling effect on the growth of multiemployer plans that has persisted in several industries despite the fact that most have had no unfunded benefits for most of that time. On the other hand, for many, the threat of unfunded liabilities provided an incentive to plan fiduciaries to adopt and follow conservative funding and investment policies that, in combination with a robust economy, led the plans to become fully funded.

Nevertheless, rather than being able to build a buffer against future economic downturns, this success led plans to experience problems at the top of the funding spectrum. In the late 1980s and throughout the 1990s, plans began to hit the full funding limits of the tax code. Under these provisions, employers that contribute to plans in excess of these limits were precluded from receiving current deductions for their contributions to the plans. Compounding the situation, employers who continued to make their contributions also faced an excise tax for doing so, despite the fact that the collective bargaining agreements to which they were signatory obligated them to continue to make them. Although in rare instances the bargaining parties negotiated "contribution holidays," timing considerations and the fact that in most cases the plan fiduciaries and bargaining parties were different people meant that plan trustees had no choice other than to increase plan costs by improving benefits to bring plan costs up to the level of plan income to protect the deductibility of employer contributions. Further, once adopted, many of the actions taken to improve the plan of benefits cannot be rescinded under the anti-cutback provisions of the law which have evolved since ERISA was first passed. It is estimated that over 75% of multiemployer defined benefit pension plans were forced to make these benefit improvements as a result of the maximum deductible limits. Overall, multiemployer plans were very well funded as the plans approached the end of the millennium, with the average funded position for all multiemployer plans at 97% (see The Segal Company Survey of the Funded Position of Multiemployer Plans - 2000).

In the three years that followed, however, these same plans suffered significant losses as the crisis of confidence over the accounting scandals and corporate excesses exemplified by Enron, Tyco, and WorldCom, sent the markets into a deep and prolonged contraction. For the first time since the ERISA funding rules were adopted in 1974; in fact, for the first time since before the beginning of World War II, the markets experienced three consecutive years of negative performance. Not only were plans unable to meet their long term assumed rates of return on their investments, virtually all institutional investors saw the principal of their trusts decline. For many of these mature multiemployer plans that depend on investment income for as much as 80% of their total income, the loss of significant portions of the trust caused a rapid depletion of what for most had been significant credit balances in their funding standard accounts. Although the most recent report showing the funded position of multiemployer plans shows a significant decline from the 97% in 2000, the average funded position is still relatively healthy at 84%. Nevertheless, these investment losses have left a number of plans at all levels of funding facing credit balances approaching zero, meaning these plans face a funding deficiency in the near future (see The Segal Company Survey of the Funded Position of Multiemployer Plans – 2004). According to the most recent estimates, as many as 15% of all plans are projected to have a funding deficiency by the year 2008 and an additional 13% face the same fate by 2012 (assuming benefit levels and contribution rates remain unchanged).

The implications of a funding deficiency for contributing employers, the plans and their participants are potentially devastating. Once a plan's credit balance drops below zero, contributing employers are assessed by the plan trustees for additional contributions in an amount equal to their proportionate share of the amount necessary for the plan to meet its minimum funding requirements. This is above the amounts they have contributed pursuant to their collective bargaining agreements. In addition, they are required to pay an excise tax by the IRS equal to 5% of that assessment. In the event that all contributing employers fail to make up the shortfall in a timely fashion, the excise tax may be increased to 100% of the shortage.

For many of the contributing employers, especially those in industries (like, but not limited to, construction) which traditionally have small profit margins, they have bid their work throughout the year based on their fixed labor costs (including the negotiated pension contributions). For them, receiving an assessment for what could be multiples of the total contributed for the year, could be enough to drive them into bankruptcy. In this instance, the concept of pooled risk among contributing employers means that the shortage amounts as well as the excise taxes owed by the bankrupt employers would be redistributed among the remaining employers, invariably pulling some at the next tier into a similar fate. As more and more employers fail, those companies that are more financially secure begin to worry about being the "last man standing." The result is that they will also seek ways to abandon the plan before all of their assets are at risk. When all of the employers withdraw, the assets of the plan will be distributed in the form of benefit payments until the assets on hand are sufficiently depleted to qualify for assistance from the PBGC. At that point, participants' benefits will be reduced to the maximum guaranteed levels, as noted above, which are likely to represent only a fraction of the amount to which they would otherwise be entitled at normal retirement age.

A Balanced, Negotiated Industry-Wide Response

Trustees of most plans faced with the prospects of an impending funding deficiency have already taken action to address the problem to the extent possible. For the most part, that has involved reducing future accrual rates or ancillary benefits that have not yet been accrued, as the current anti-cutback regulations prohibit reducing benefits that have already been accrued. In many cases, this has involved substantial reductions (e.g. 40% by the Western Conference of Teamsters, 50% by the Sheet Metal Workers National Pension Plan and the Central States Teamsters Pension Plan, and 75% in the case of the Plumbers and Pipefitters National Pension Plan). But because the financial impact of adjusting only future benefits can be limited, these actions on their own may be insufficient to avoid a funding deficiency. Additionally, the modest recovery of the investment markets experienced in 2004 is only marginally helpful. For example, a $1 billion fund in 2000 that suffered a 20% decline in assets through 2003 would have to realize an annualized rated of return of 15% every year for the remainder of the decade to get to the financial position by 2010 it would have had it achieved a steady rate of 7.5% for the full ten year period. Other relief, including funding amortization extensions under IRC Section 412(e) or the use of the Shortfall Funding Method, have been effectively precluded as options by the IRS. Consequently, the only alternative available requires a legislative solution.

Following the failed attempt at relief in the Pension Funding Equity Act of 2004, various groups began to evaluate alternatives that might help plans get by avoidable situations, while attempting to help plans that were placed at risk by unavoidable external forces. The objective was to find ways to provide additional tools to the plan fiduciaries and bargaining parties for plans that face imminent funding deficiencies to bring liabilities and resources into balance. From April 2004 through early May 2005 a broad cross section of groups, including those that were on different sides in the earlier debate, entered into extensive negotiations to develop a set of specifications for reform that the full group could agree on. The specifications for reform that resulted from those negotiations reflect a carefully conceived compromise between employer and labor groups, undoubtedly quite different from what either group would have designed independently, but reflective of a desire by all parties to preserve the plans and the maximum benefits payable to plan participants today and in the future. That initial group was expanded through meetings with numerous employer and labor groups and the result was the current coalition proposal, a copy of which is included as an addendum to this testimony. A summary of that proposal is as follows:

Summary of Coalition Proposal

The proposed specifications for multiemployer reform is comprised of three major components and supplemented with several clarifying and remedial changes intended to make the system work more effectively for plans, their participants and sponsors.

The first component is applicable to all plans and has two major provisions geared to strengthening funding requirements for plan amendments that increase or decrease plan costs (specifically unfunded actuarial accrued liabilities) related to past service and to shorten the amortization of costs for improvements that are to be paid out over a shorter period to the payment period.

The other major provision would allow plans to build a "cushion" against future contractions in the plan's funded position by increasing the maximum deductible limit to 140% of the current limits and would repeal the combined limit on deductions for multiemployer defined benefit and defined contribution plans.

The second component applies to plans that have potential funding problems, defined in the coalition proposal as being plans that have a funded ratio of less than 80% using the market value of assets compared to the actuarial value of its actuarial accrued liability. Such plans would be required to develop and adopt a "benefit security plan" that would improve the plan's funded status. Plans in this category would not be able to adopt amendments to improve benefits unless the additional contributions related to such amendment more than offset the additional costs to the plan. Amendments that violate that restriction would be void, the participants would be notified and the benefit increase would be cancelled.

To provide additional tools to plans to avoid funding problems, plans would have “fast track” access to five year amortization extensions and the Shortfall Funding Method if certain criteria were met. IRS authorization could be withheld only in certain circumstances and applications would need to be acted upon within 90 days or the approval would be automatic. Additional restrictions that currently apply to plans with amortization extensions would also apply.

The third and most critical component involves plans that have severe funding problems or will be unable to pay promised benefits in the near future. The clear intent of this provision is to prevent a funding deficiency that could trigger a downward spiral of the plan and its contributing employers and a reduction in the ultimate benefit payable to the PBGC guarantee levels. This is accomplished by providing the bargaining parties with additional tools beyond those currently available to bring the plan’s liabilities and resources back into balance.

The proposal modifies the current reorganization rules to provide a meaningful option to plan sponsors, much like a Chapter 11 bankruptcy reorganization. ERISA currently has reorganization rules governing plans that are nearing insolvency, but those rules were adopted at a time when the major concern was a plan’s ability to meet its payment obligations to current pensioners. Today, even those plans with the most severe funding problems have sufficient assets to meet their obligations to current pensioners. The coalition proposal suggests several new triggers to reorganization that reflect the problems of mature plans, recognizing that funding ratios below 65%, a plan’s short term solvency and a plan’s demographic characteristics (i.e. the relationship between the present value of benefits earned by inactive vested and retired participants to that of currently active participants) can play an important role in a plan’s ability to meet its obligations to all participants, current and future.

Once a plan is in reorganization, notice would be given to all stakeholders and the government agencies with jurisdiction over the plans that the plan is in reorganization and describing the possible consequences. Once in reorganization, plans would be prohibited from paying out full or partial lump sums, social security level income options for people not already in pay status, or other 417(e) benefits (except for the $5,000 small annuity cash outs). Within thirty days, contributing employers would be required to begin paying a surcharge of 5% above their negotiated contribution rates. If the bargaining agreement covering such contributions expires more than one year from the date of reorganization, the surcharge would increase to 10% above the negotiated rate and remain there until next round of bargaining. Once in reorganization, the normal funding standard account continues to run, but no excise taxes or supplemental contributions will be imposed if the plan encounters a funding deficiency.

Not later than seventy-five days before the end of the first year of reorganization, the plan fiduciaries must develop a rehabilitation plan to take the plan out of reorganization within ten years. The plan would set forth the combination of contribution increases, expense reductions (including possible mergers), benefit reductions and funding relief measures (including amortization extensions) that would need to be adopted by the plan or bargaining parties to achieve that objective. Annual updates to the plan of rehabilitation would need to be adopted and reported to the affected stakeholders. Although the proposal anticipates the loosening of the current anti-cutback rules with respect to ancillary benefits (such as subsidized early retirement benefits, subsidized joint and survivor benefits, and disability benefits not yet in pay status), a participant's core retirement benefit at normal retirement age would not be reduced. Additionally, with one minor exception which follows current law regarding benefit increases in effect less than 60 months, no benefit for pensioners already in pay status would be affected. Finally benefit accruals for active employees could not be reduced below a specified "floor" as a means of ensuring that the active employees whose contributions support all plan funding, remain committed to the plan.

The proposal anticipates that these ancillary benefits become available as part of a menu of benefits that can modified to protect plans from collapsing under the weight of previously adopted plan improvements that are no longer sustainable, but that cannot be modified under the current anti-cutback restrictions. Without such relief participants would receive lower overall benefits on plan termination and the plan would be eliminated for future generations of workers. Within seventy-five days of the end of the first year a plan is in reorganization, the plan trustees must provide the bargaining parties with a schedule of benefit modifications and other measures required to bring the plan out of reorganization under the current contribution structure (excluding applicable surcharges). If benefit reductions alone are insufficient to bring the plan out of reorganization, the trustees shall include the amount of contribution increases necessary to bring the plan out of reorganization (notwithstanding the floor on benefit accruals noted above). The trustees shall also provide any other reasonable schedule requested by the bargaining parties they deem appropriate.

The bargaining parties will then negotiate over the appropriate combination from among the options provided by the trustees. Under this proposal, benefits for inactive vested participants are subject to reduction to harmonize the impact on future benefits for this group as well as for active participants.

The proposal includes suggestions for: bringing the current rules on insolvency in line with the proposed reorganization rules; strengthening withdrawal liability provisions; and providing construction industry funds with additional flexibility currently available to other industries to encourage additional employer participation. It also addresses recent court rulings, with one amendment that allows trustees to adjust the rules under which retirees can return to work and still receive their pension benefits and another that permits plans to rescind gratuitous benefit improvements for current retirees adopted after the date they retired and stopped generating employer contributions.

Conclusion

For more than half a century, multiemployer plans have provided benefits for tens of millions of employees who, using standard corporate rules of eligibility and vesting, would never have become eligible. They offer full portability as workers move from one employer to another in a system that should be held out as a model for all defined benefit plans. More importantly, the system of collective bargaining and the checks and balances offered by joint employer –

employee management has enabled the private sector to take care of its own without the need for government support.

Yet the current funding rules, previously untested under the unprecedented unfavorable investment climate experienced in recent years, have the potential not only to undermine the retirement income security of millions of current and future workers and their dependents, but to force large numbers of small businesses out of business and eliminating participants' jobs.

The United States Senate and House of Representatives have been presented with an ideal opportunity to enact meaningful reform supported by both the employer and employee community who have coalesced behind a responsible proposal that will enhance plan funding and provide safeguards to plans, participants, sponsoring employers and the PBGC, without adding to the already burgeoning debt. Although the proposal includes certain provisions that are distasteful to both parties, it is a compromise product of careful negotiations by employers and the employees' legally recognized representatives. The alternative is not the continuation of the status quo, but a much worse fate that includes: the loss not only of accrued ancillary benefits, but a substantial portion of a participant's normal retirement benefit as plans are assumed by the PBGC; the demise of potentially large numbers of small businesses and the loss, not only of pension benefits, but the jobs from which such benefits stem; and an increase in taxpayer exposure at the PBGC, an agency that is already overburdened.

We urge the Committee to wholeheartedly support this proposal and look forward to working with you to see it enacted into law.

In closing, I would like to thank you for taking the time to engage in this important discussion and for the opportunity to be with you here today.