NATIONAL COORDINATING COMMITTEE FOR MULTIEMPLOYER PLANS

815 16TH STREET, N.W., WASHINGTON, DC 20006 • PHONE 202-737-5315 • FAX 202-737-1308

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Committee on Education and the Workforce

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Examining Reforms to Modernize the Multiemployer Pension System

Testimony of:

Randy G. DeFrehn, Executive Director
National Coordinating Committee for Multiemployer Plans (NCCMP)

Chairman Roe, Ranking Member Polis and Members of the Committee, it is an honor to appear before you today on this important topic. I am Randy DeFrehn, Executive Director of the National Coordinating Committee for Multiemployer Plans, an advocacy organization chartered under Section 501(c)(4) of the Internal Revenue Code, created following the enactment of ERISA to represent the interests of multiemployer benefit plans, their participants and their sponsors.

Multiemployer plans are the product of collective bargaining agreements between one or more labor unions and more than one contributing employer which require contributions to a trust to be held and administered for the sole and exclusive benefit of plan participants. While commonly associated with the construction and trucking industries, they are found across the economy including in the agriculture, aerospace, bakery and confectionery, building service, clothing, entertainment, food production, distribution and sales, health care, hospitality, longshore, maritime, mining, manufacturing, retail, textile, and transportation industries.

I would like to thank the Committee for the opportunity to appear here before you once again on the topic of multiemployer retirement security. It is also an honor to say thank you, on behalf of the more than 10 million participants in multiemployer defined benefit plans, for the bi-partisan leadership shown by this Committee and Sub-committee in the enactment of the *Multiemployer Pension Reform Act*, passed as part of the *Consolidated and Further Continuing Appropriations Act 2015*, which was signed into law last December.

That legislation addressed two of the three major categories of recommendations of the Retirement Security Review Commission (or Commission), a broad based consortium of stakeholders representing more than 40 stakeholder groups including labor unions, employer associations, large plans, large individual employers and advocacy organizations from industries across the multiemployer community. For a period of eighteen months this group met to review the strengths and weaknesses of the multiemployer defined benefit pension system and formulate recommendations designed to weather its current challenges and to facilitate its success in the future. These categories included recommendations to preserve the financial health of the more than two-thirds of plans which have already, or will soon regain their financial stability following the back-to-back recessions since 2000, including technical corrections to the Pension Protection Act; and recommendations to preserve plans headed for insolvency and preserve benefits for participants in such plans above levels they would have otherwise ultimately received under prior law.

The third category of recommendations from the Commission remaining to be addressed concerns innovative new benefit structures designed to address the shortcomings of both the current defined benefit or defined contribution plans. It is the need for this remaining set of reforms that I am here to address today.

Background

For over seventy years, multiemployer defined benefit pension plans have provided tens of millions of American men and women and their families with regular, though modest retirement income which, along with Social Security and personal savings, have allowed them to retire in dignity. Since the PBGC multiemployer guaranty fund was initiated in 1980, the number of plans has declined from slightly over 2,200, consistent with the decline in defined benefit plans in corporate America. Contrary to that trend, however, the number of covered participants has increased from 8 million to over 10 million, largely due to the mergers of many smaller funds into larger ones. According to the PBGC, approximately 1,350 multiemployer defined benefit plans cover approximately 10.4 million active, retired and terminated vested workers. Defined benefit plans continue to be the primary retirement plans for multiemployer participants, with defined contribution plans being used as supplemental income plans.

Over that period, multiemployer plans have gone through a number of evolutionary changes. They began as true "union plans," but were subsequently replaced in favor of equal labor-management plans with the passage of the Taft-Hartley Act. These pay-as-you-go plans were then forced to pre-fund when ERISA was passed. Many employers believed that since only the contribution rates are negotiated, these plans were defined contribution until the late 1970's when the Supreme Court ruled in Connolly v. PBGC that they are defined benefit plans.

While ERISA provided for the creation of the PBGC to provide a safety net for plans in industries that fail, the multiemployer plan guaranty fund was not implemented until the passage of the Multiemployer Pension Plans Amendment Act of 1980. A second aspect of that legislation was the creation of withdrawal liability – in essence, an exit fee – to be paid by employers who withdraw from plans with unfunded vested benefits. While theoretically a sound idea, industry specific limitations on when this fee is imposed, the 20 year cap on the amount ultimately imposed, amounts excused by bankruptcy courts and departures of small employers that are judgment-proof have resulted in recovery of less than 10% of assessed liabilities and have made withdrawal liability more of a hindrance than a help to the long-term financial health of plans by creating a barrier to new employers that might otherwise join the system.

When this fee was first imposed, it was forecast by some to be the end of multiemployer plans; however, a combination of conservative benefit payments, an expanding economy and robust investment markets soon made unfunded liabilities a thing of the past for the vast majority of plans. Instead the focus of attention for most plan sponsors shifted to the part of the tax code which limited the current deductibility of contributions to over funded plans. The remedy for the vast majority of plans was to increase benefit payments to preserve the current deductibility of contributions. While effective for addressing the immediate problem these actions also increased recurring plan liabilities prior to the inevitable market corrections and re-emergence of unfunded liabilities that followed soon after the turn of the century.

To compound the problem, additional financial disclosures required by the Financial Accounting Standards Board (regardless of the potential for incurring such liability) imposed after the 2008 recession has resulted in the downgrading of the credit rating of at least one publically traded firm and has had an adverse effect on the ability of other contributing firms to access credit markets. These new rules have made a bad situation worse by making it nearly impossible to bring new contributing employers into the contribution base in many industries. Without the influx of new employers, plans will be destined to deal with a continually contracting base of contributing employers – a prospect that has dire implications for the long-term viability of many such plans.

For the majority of industries and employers, multiemployer defined benefit plans have recovered or are on a path to recovery from the devastating losses of the past decade and will continue to be the norm. For others, the MPRA has provided a life line for plans and their participants for those plans that choose to utilize the new tools that have become available.

For still other employers, however, these recent past developments have left them feeling that the current structure presents an unacceptable risk of recurrence, causing them to seek other forms of pension coverage for their employees. For these employers, the only alternative is a defined contribution plan based on an individual account. As a primary form of retirement security vs. a wealth accumulation process, however, defined contribution plans present certain inefficiencies which may result in lower ultimate benefits for average workers, many of which are vexing even to those of us who specialize in retirement policy matters, including assuming the responsibility for making correct investment choices, paying the lowest possible fees and in estimating life expectancy.

To the Commission this resulted in yet another challenge: how to find an alternative plan design for the future that would reduce or eliminate the risks of unfunded liabilities to the employers, yet addresses the shortcomings of the current defined contribution system so that workers can continue to receive a regular monthly retirement income and maximize the utility of employer contributions without requiring each participant to take on responsibilities of actuary and investment manager for which they are ill equipped. The result of their analysis was a recommendation to encourage the development and approval of innovative, “shared risk” plan designs, offering two different models: the variable defined benefit and the composite (or target plan as it was described in the Commission’s report) as illustrative rather than finite solutions for the future. As the variable defined benefit model has already been adopted and, in at least one situation received a tax qualification letter from Treasury, my comments here will focus on the composite model.

The composite plan is neither a defined benefit, nor defined contribution plan under the current statutory structures as the variable nature of the benefit is neither definitely determinable, nor is it based on an individual account. It would be made available to jointly managed, multiemployer plans as a successor plan to their current defined benefit plan. The model includes very clear conditions for the parties to pay off the liabilities of the “legacy” defined benefit plan as the first priority for contributions. It also requires that contributions to fund future accruals be subject to a higher funding standard than are required for the current defined benefit plans. If the parties so desire, the benefit plan design could mirror the current plan design for the defined benefit plan. It could also continue many of the more favorable features of defined benefit plans. From the participants’ perspective, this new structure will provide higher monthly benefits than would be derived from simply purchasing an annuity from his or her account balance in a defined contribution account. This can be accomplished in several ways including through the pooling of longevity risk, and by limiting other features that result in plan leakage and ultimately lower retirement income such as loans, hardship distributions, distributions before retirement and lump-sum distributions, as benefits would be required to be paid as annuities.

This new structure is clearly not a defined benefit plan, however, as benefits are variable based on the market value of assets (as currently happens with defined contribution plans). The amount one would receive would be adjusted on an annual basis to mitigate the frequency and impact of market fluctuations, projected for a fifteen year period. As it is not a defined benefit plan, service earned after adoption would not be subject to PBGC guaranty, nor would employers be subject to withdrawal liability. Both of these features would remain in place, however, for remaining obligations under the legacy plan.

Contributions to both plans would be determined by the plan’s actuary however, as the market risk for future service rests with the participant, the minimum contribution requirement to fund the cost of future accruals would be set at 120% of the actuarial projected costs to provide a buffer against market volatility. Each year the plan would conduct an actuarial valuation to determine whether the assets were sufficient to meet that funding projection over a fifteen year period. Assuming the plan continues to meet that target, no action would be necessary and, if a sufficient margin were to develop, the plan trustees could consider possible benefit improvements, provided that such improvements do not reduce the projected funding below the 120% target. If, however, the projections fall below the 120% target, the trustees would be required to take remedial action within 210 days of the date of the certification of plan funding based on a clearly defined hierarchy.

If the asset decline is modest, the parties would negotiate additional contributions, or the trustees could adjust the value of future accruals, much the same as is currently done for defined benefit plans. Because this is not a defined benefit plan, however, in the event projected plan assets fall more precipitously, action would be required to adjust benefits for all participants to return the plan to the required funding level. Benefits that could be adjusted include those that are not considered "core" benefits – normal retirement benefits payable at normal retirement age – such as post-retirement benefit improvements, subsidized early retirement or surviving spouse benefits or other benefits that are currently adjustable for critical status plans under the PPA.

In the event of a catastrophic market event, rules similar to those for defined benefit plans in critical and declining status plans would be imposed in order to restore required funding.

Conclusion:

In the past few years much as been made of the need to improve the retirement security of workers. Both the Departments of Labor and Treasury have embarked upon a program to encourage lifetime income to participants in defined contribution plans. This body has taken bold action to preserve the long-term solvency of multiemployer plans in last year's passage of MPRA. Yet there remains one last aspect reform to be enacted.

For some, the composite plan is the next logical step in the evolution of collectively bargained multiemployer plans. For those who are no longer willing to assume the risk of ensuring the performance of the investment markets, yet are genuinely concerned that many if not most of the workers covered by multiemployer plans do not possess the income levels, sophistication or discipline to accumulate sufficient wealth in a traditional defined contribution plan to meet the lifetime income objective (a concern that is not limited to this population but shared by many in the retirement community), the composite plan provides the best of both worlds. If enacted, the structure and safeguards will provide greater long-term retirement security by creating a path for contributing employers to remain in and new employers to enter the multiemployer system without presenting existential risks, while providing the greatest possible benefit for covered participants.

I thank you for the opportunity to share these thoughts and welcome any questions you may have.

Respectfully submitted,

Randy G. DeFrehn
Executive Director