Statement
of
The ERISA Industry Committee

Submitted to
U.S. House of Representatives
Committee on Ways and Means

Hearing on
Defined Benefit Plan Funding Levels
and
Investment Advice Rules

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The ERISA Industry Committee
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Regarding
Defined Benefit Plan Funding Levels
and
Investment Advice Rules

As the representative of America's major employers on retirement issues, The ERISA Industry Committee ("ERIC") appreciates the Committee's focus on the issues of funding relief for pension plans and investment advice in defined contribution plans.

ERIC is a nonprofit association committed to the advancement of the employee retirement, health, incentive, and welfare benefit plans of America's largest employers. ERIC's members provide comprehensive retirement, health care coverage, incentive, and other economic security benefits directly to some 25 million active and retired workers and their families. ERIC has a strong interest in proposals affecting its members' ability to deliver those benefits, their costs and effectiveness, and the role of those benefits in the American economy.

SUMMARY: DEFINED BENEFIT PLAN FUNDING RELIEF

ERIC strongly supports and has urged both the Congress and the Administration to provide immediate, temporary and meaningful funding relief for defined benefit plans. Employers have not asked and are not now asking for relief in the form of direct financial support from the government. Rather we are merely asking for more time to make unexpected and larger contributions to defined benefit plans as a result of the unprecedented financial and economic problems that stem from the ongoing global financial meltdown.

Companies that sponsor defined benefit plans, including those that had made significant contributions to comply with the new more stringent funding rules of the Pension Protection Act of 2006 (PPA), suffered significant and unexpected losses in their pension plan investment portfolios as a result of the "once in a generation" investment crisis. Because of the worst recession since the Great Depression, many have been forced to freeze their pension plans, reduce financial support for 401(k) plans, curtail employment, and significantly reduce investment.

Unlike other sectors of the economy, however, companies sponsoring defined benefit plans are not asking for a taxpayer bailout; instead we are merely asking for more time to make contributions to match long-term liabilities inherent in the pension plan system. There is ample precedent for such a solution: in 1974 when the Employee Retirement Income Security Act (ERISA) was enacted, companies were given 30 years to amortize existing liabilities.

SUMMARY: PARTICIPANT ADVICE

Millions of Americans rely on their 401(k) plan and other defined contribution plans for retirement security. ERIC member companies who sponsor 401(k) plans offer investment advice products and services to plan participants as permitted under current law. Many utilize the regulatory framework approved by the Department of Labor known as "SunAmerica," whereby participants receive investment advice based on a computer model designed by a third party with no financial stake in the underlying investments in the plan and is independent of the service provider or financial institution providing the investment advice.

ERIC supports investment advice rules that carefully balance the need of the participant to receive effective and useful investment advice from the company plan sponsor and/or its service provider as well as the need for the employer to have clear and consistent rules under which to legally offer the advice. ERIC's members have a vital interest in assuring that the rules and regulations issued in connection with investment advice achieves its objective <u>in a way that encourages voluntary investment advice programs without exposing employers to an undue risk of fiduciary liability</u>.

Defined Benefit Plan Funding

As Congress and the Administration focus on efforts to stimulate the economy, real relief for America's pension plans is an absolute necessity. There is general agreement among those directly concerned with business, employment, and retirement administration that failure to provide meaningful relief will increase unemployment, slow economic recovery, and put retirement security at risk. The drop in the value of pension plan assets and the credit crunch, together with the new accelerated funding requirements of the Pension Protection Act of 2006 (PPA), has placed employers in a difficult position.

At a time when companies need cash to keep their business afloat, retain and recruit employees, build product in American factories, the new funding rules under the PPA coupled with the economic meltdown require extraordinary and unexpected cash contributions to their defined benefit plans, to fund liabilities that are many years in the future.

As a result, companies, including those that need to continue to manufacture goods and build inventory, will divert much needed cash to make pension plan contributions, cash that would otherwise be spent on current job retention, job creation, and capital investments. Many of these companies fear that they will be forced to increase off-shore resources – with its permanent impact on jobs - in order to reduce costs to make up for these contributions. These funding challenges apply to both frozen and non-frozen plans (those that continue to accrue new benefits for employees). Unless Congress intercedes with reasonable rules that will promote retention of pension plans, the result will be an increase in unemployment – some of it permanent - and a slower economic recovery.

The Worker, Retiree, and Employer Relief Act of 2008 corrected a number of technical errors in the PPA and clarified some points of contention between plan sponsors and the regulatory agencies. It did not, however, adequately provide the substantive relief needed to force plan sponsors from making an unfortunate choice between funding their pension plans and retaining current employees, hiring new employees, and the capital investments necessary to stimulate the economy and improve the lives of millions of Americans.

The Treasury Department has recently provided some needed regulatory relief in this area. However, due to statutory constraints, the Treasury relief was not provided to all pension plans, leaving some plans, particularly fiscal-year plans (as opposed to calendar-year plans) suffering grave economic hardship. Simply stated, Congress needs to act, quickly and decisively in order to support the remaining defined benefit plans still offering retirement security to participants. Any relief that Congress provides must be made available to both frozen and non-frozen plans in order help companies transition out of this deep recession.

As you are aware, the last four months of 2008 posed a significant challenge for defined benefit pension plans that, in compliance with the PPA 2006, had reached or were close to full funding. A dramatic and unexpected decline in the value of the equity markets significantly reduced the assets held by these plans through no fault of the. As a result, pension plans that were fully funded only one year ago are now substantially underfunded under the standards set by the PPA 2006.

The PPA significantly tightened the nation's pension funding rules. Congress, not anticipating the financial crisis, made no provision in the Act that that would have provided relief from the crisis. Plan sponsors have spent the two-plus years since the legislation was enacted preparing to meet the new law's funding requirements, but they, like Congress when the law was enacted, did not and could not anticipate the financial crisis through which the nation is now progressing. The confluence of tighter funding laws and the current economic environment created a "perfect storm" that requires relief.

Many major employers that have responsibly funded their pension plans are now facing statutorily required contributions in the coming year that exceed the previous year's contributions by magnitudes of hundreds of percent. The sheer size of the contributions leaves employers in an untenable position: they must either cut jobs and delay hiring and investment, or allow their plans to go underfunded, in many cases, resulting in restrictions on the benefits that workers can claim as they retire. In some cases, the pension liabilities that must be met under the requirements of the PPA may exceed the net worth of the company. We do not believe that Congress intended to allow companies to close their doors as a result of inability to meet the funding requirements of the PPA coupled with the Great Recession.

Looking ahead to 2010, companies expect increased required contributions to their pension plans, barring an enormous market recovery or another unusual spike in interest rates that would reduce minimum contributions. These increased minimum contributions apply to both frozen and non-frozen plans because of investment losses and interest rate assumptions.

Because companies suffered enormous investment losses in 2008, current investment returns are not sufficient to reverse the dramatic negative investment returns of the last quarter of 2008. Those losses, the low return on investments, coupled with the fact that interest rates are substantially lower than in October 2008, results in an increase in the computation of pension plan liabilities (based on current interest rates). Higher liabilities result in higher minimum contributions to the plans, thus continuing the cash-crunch cycle into 2010 and forcing companies to choose between funding pension plan trust funds, that represent long-term liabilities, and ending workforce reductions, rehiring workers and/or making infusions of capital into their core business interests.

A failure to provide funding relief will undoubtedly have real pension implications including an increased risk to the PBGC and the loss of pension benefits and plan freezes (as well as curtailment of 401(k) plans in order to raise cash) for many workers, the repercussions will stretch far beyond pensions to the whole of economic growth. With required contributions for many employers reaching tens and hundreds of millions of dollars, the job and investment consequences of failing to act are real. We urge you to provide real, temporary relief that allows plan sponsors additional time to fully fund their pension plans.

Pension plan sponsors are not asking for a bailout—we are not asking that the government provide plan sponsors with cash or take on plan sponsors' liabilities. ***Plan sponsors simply need additional time over which to make their pension contributions.*** Plan sponsors need more time to amortize the 2008 losses as well as rules that reflect the true long-term nature of the pension plan liability.

In these uncertain economic times, employers are forced into making hard and difficult choices – in some cases cutting retirement benefits in order to retain jobs. Many employers eliminated 401(k) matches in order to divert the cash to cover other expenses, including payroll, and defined benefit plan funding. These employers hope to and in some cases are slowly returning to providing the employer match. However, as we have learned from this economic crisis, employers need the flexibility to make business decisions regarding cash allocation quickly and without depending on Congress.

One short-term result of the economic crisis, and government failure to date to provide needed flexible relief, is that employers are hesitant to take on long-term financial commitments. For instance, employers are wary of making long-term commitments that require maintenance of short term funding to cover what are in fact, long term liabilities. The current financial crisis not only impacts workers today, but also will have severe, short-term negative effects on the pension plans in which they participate, reducing benefits, undermining retirement security and will continue to impact the ability for large employers to maintain current workforce levels.
We understand that there are some, in and out of government, who contend that there are no econometric studies to illustrate that if companies are required to make statutorily required pension contributions they will be forced to curtail spending for jobs and investment. We find this contention so out of balance with common sense that it is without merit of consideration.

Investment Advice

The Education and Labor Committee approved a bill this summer that would drastically change the way employers offer investment advice to workers participating in their 401(k) plans. The PPA included investment advice provisions that expanded the ways in which employers could provide investment advice to their workers through their 401(k) plans. The effective date of the final regulations on investment advice issued by the Bush Administration has been delayed upon further review by the Obama Administration.

Employers need clear rules that apply when an employer chooses to make investment education or investment advice available under a participant-directed defined contribution plan. Congress should recognize, however, that plan sponsors and fiduciaries are increasingly targeted in class action lawsuits that propose expansive theories of fiduciary liability and seek substantive damages. Even when these lawsuits are without merit, as is often the case, they are expensive to defend and they divert time and attention from the employer's business. As a result, any employer that considers whether to adopt an investment advice program must weigh the potential benefit to plan participants against the very real risk of costly and time-consuming litigation.

Employers will voluntarily offer investment advice programs only if the rules governing these programs are clear and objective, do not open the door to increased fiduciary liability, and provide safe harbors whenever possible.

The Education and Labor's bill approved out of the Committee this summer, would significantly disrupt the manner in which employers provide investment advice to plan participants. Specifically, this legislation would prohibit employers from providing investment advice under most "SunAmerica" models, which has provided a framework for employers to provide investment advice for eight years.

Many ERIC members provide investment advice under the SunAmerica model. Our members have indicated that if the rules under which employers may offer participants investment advice in 401(k) plans are completely revamped so as to preclude most SunAmerica arrangements, many would not undertake the expensive and time-consuming exercise of overhauling their investment advice programs. In addition, these changes would also result in uncertainty and increased exposure to liability for employers.

ERIC strongly supports the SunAmerica investment advice framework. It appears that the Education and Labor Committee has concerns regarding the PPA investment advice provision as well as the Bush Administration final regulations on investment advice. ERIC urges a full and fair debate on this issue within the Committee. However, by casting doubt on SunAmerica arrangements, Congress would force employers to review and reconsider whether providing investment advice results in litigation jeopardy. Employers would limit and or eliminate investment advice programs resulting in fewer Americans receiving investment advice through their employer-sponsored 401(k) plans.

ERIC appreciates the opportunity to present this statement. If the Committee has any questions about our statement for the record, or if we can be of further assistance, please let us know.