Opening Statement by Rep. John Boehner (R-OH), Chairman,
Committee on Education and the Workforce

Hearing on
Examining Cash Balance Pension Plans: Separating Myth from Fact

July 7, 2004

I'd like to thank everyone for coming to the eighth in our series of hearings on defined benefit pension plans for a topic that is particularly timely. Cash balance plans have received a lot of attention recently, producing rhetoric that has often been misleading if not false. Today, we hope to separate myth from fact.

As we all know the number of defined benefit plans has declined significantly over the last 20 years, from 114,000 in 1985 to 31,000 last year, and the entire defined benefit system remains at risk. Some experts have suggested that cash balance plans, which are a type of defined benefit plan, offer today's workers the type of secure and portable benefit that can help save and preserve the overall system. Unfortunately, fewer and fewer companies are offering cash balance plans because of a recent wave of litigation.

Before I talk about this specifically, I'd like to discuss some facts about how these plans work. Under cash balance plans, workers earn portable benefits through monthly pay and interest credits, and benefits are earned more evenly over a career span, not just at the end of a worker's career. This can result in greater retirement savings for workers who do not remain with the same employer for their entire career. As a result, a broader group of employees – including lower-income workers and women – earn greater benefits with shorter service under cash balance plans than traditional plans. According to a study published by Watson Wyatt in 2000, more than 80 percent of participants fare better with a cash balance plan.

The value of the benefit in a traditional plan spikes for workers who qualify for an early retirement subsidy, typically in their mid-50s, but then declines if they fail to retire at a specific age and keep working. As a result, traditional plans are advantageous only for the small proportion of employees who work for the same employer for 20 to 30 years AND retire in their mid-50s. Conversely, traditional plans are disadvantageous for younger employees, for workers who change jobs or interrupt their careers, and for older workers who continue working after early and normal retirement age.

The Employee Retirement Income Security Act (ERISA) prohibits employers from cutting back or reducing any pension benefits that have been earned by employees once they vest in their pension plan. Despite this current law protection, some critics have continued to express concern over cash balance conversions despite the fact a large majority of them have been handled properly and legally.

The real issue here is about a small number of prospective retirees' expectation of receiving the full value of early retirement subsidies that have not yet been earned. This is not about normal retirement benefits. Rather, I'm concerned that cash balance critics are focused not on providing meaningful retirement benefits to our overall workforce, but solely on protecting a small fraction of employees who can afford to retire early. It is important to note that under the voluntary pension system all defined benefit plan sponsors may change benefit formulas prospectively to either enhance or reduce future benefits that have not yet been earned by an employee. All employers need the flexibility to determine what is appropriate for the needs of their workers and their business. If this flexibility is taken away or if Congress were to unilaterally mandate certain pension benefits, employers would leave the voluntary pension system altogether and the defined benefit system would all but disappear.

The recent wave of litigation surrounding cash balance plans has raised concerns from employers, workers, and policymakers alike. One well-documented court case involves IBM, but the initial ruling runs counter to existing law and a large body of other court decisions. In this case, the judge found the cash balance plan design inherently age discriminatory because equal pay credits for younger workers have a longer period of time to earn interest and accrue benefits before retirement than the same pay credits for older workers. This interpretation essentially means it would be age discriminatory to make equal contributions on behalf of workers with different ages. This is inconsistent with every other pension design and this logic would make a basic savings account, 401(k) plans, and even Social Security benefits automatically age discriminatory. We're not here to debate the IBM case, but we also need to make sure cash balance plans aren't forced into extinction at the expense of the interests of workers.

Most courts have ruled no age discrimination occurs with cash balance plans if the pay and interest credits given to older employee accounts are equal to or greater than those of younger employees. The most recent ruling on this topic, issued just last month in the Tootle case, agrees that cash balance plans are not inherently age discriminatory.

I'd like to dispel another myth about these plans. The switch to cash balance plans is not motivated by cost savings, but rather pressures imposed by an increasingly mobile workforce as well as fierce competition. Under current law, employers can freeze or terminate their traditional plan without the complexity or expense of converting to a cash balance plan, and most actually spend more on retirement benefits after the conversion as before. In a world where most employees will not spend 20 to 30 years working for the same employer, the steady accrual of benefits under a cash balance plan provides greater retirement security than the distant accrual of back-loaded benefits under a traditional plan.

Our ultimate goal is to ensure cash balance plans remain a viable option for employers who want to remain in the defined benefit system and workers who prefer the portable and secure benefit this option provides. It's my hope we can move forward with reforms to strengthen cash balance plans for all workers as we craft a comprehensive proposal to reform and strengthen the defined benefit pension system. With that, I look forward to hearing from our witnesses and working with my colleagues on this issue as we move ahead.

#####