THE ERISA INDUSTRY COMMITTEE

Representing the Employee Benefits Interests of America's Largest Employers
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PRINCIPLES GOVERNING PENSION FUNDING AND FINANCIAL DISCLOSURE TO PARTICIPANTS

At a time when members of the Baby Boom cohort are entering their retirement years, the government should assist employers who voluntarily sponsor retirement plans for their employees. Meeting the nation's retirement income needs is an important public policy objective that cannot be met by reliance on government, employers, or individuals alone. Employers offer several different forms of retirement savings vehicles, among them traditional and hybrid defined benefit pension plans in which employees accrue benefits without incurring the risk of investment loss. These plans remain vital to the ability of individuals to achieve financial security in retirement.

Regulatory Environment: The federal government must create a regulatory environment that encourages the establishment, continuation, and long-term viability of defined benefit pension plans by providing plan sponsors with the certainty they need regarding –

* the interest rate used to calculate their liabilities;
* rules that support predictable and stable plan funding
* the validity of cash balance and other hybrid plan designs;

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In addition, rules governing pension plans must balance the interests of participants and of employers who voluntarily sponsor defined benefit plans. They must recognize the differences and need for flexibility among employers in plan design and the varying needs and interests of different workforces. Specifically:

* Legislation must be enacted as soon as possible that establishes a realistic and permanent interest rate assumption that appropriately measures the present value of pension plan liabilities and that, with an appropriate phase in, is applied to the minimum amount of any lump-sum distribution that a pension plan makes. The failure to change the current rate applicable to lump sums has resulted in lump sum distributions that are outsized relative to economic reality and the plan's funded status and has created an artificial incentive for participants to take their benefit in a lump sum.

* Pension funding standards must strike the appropriate balance that encourages employers both to establish and maintain defined benefit pension plans and to fund the plans on a reasonable and appropriate basis, thus protecting participants. This is essential to protecting the financial health of the pension system and the business vitality of plan sponsors. For example, legislation imposing additional requirements or benefit restrictions on plans less than fully funded should not be triggered by the credit rating of the sponsoring employer. This measure creates too

many "false positives." It would impose unnecessary burdens on a large number of employers who otherwise are not likely to terminate their plans, making their business recovery more difficult and in some cases triggering the very plan termination that the funding rules should seek to avoid.

* Employers must not be discouraged from developing new plan designs that meet the changing needs of the current and future workforce. Legislation must be enacted that confirms the legality and facilitates the adoption and continuation of hybrid plans so that employers will be more likely to continue to offer pension plans.

* The Pension Benefit Guaranty Corporation (PBGC) must align its objectives with those of employers and participants since a flourishing private pension system is the best guarantee of the PBGC's long-term viability. In other words, as required under ERISA, PBGC must set policies and act to encourage the establishment and continuation of voluntary defined benefit plans. Plan funding and premium policies should not force employers out of the voluntary pension system prematurely and unnecessarily during periods of financial distress or normal economic downturns.

Funding Objectives: In order to ensure that employees will receive pension benefits from employer-sponsored plans, the primary objectives of funding standards must be to foster plan continuation through actuarially sound funding and to allow plan sponsors to anticipate systematic and stable funding over time.

* Required contributions must be both predictable and stable in order to facilitate capital planning in the sponsoring business.

* Funding standards should permit the pre-payment of contributions when sponsors are able to do so.

* Funding standards must allow and facilitate diversification of investments of pension plan assets, including investments in equities, in order to ensure the growth and security of the plan.

* Funding standards must recognize the on-going and long-term nature of pension plans; the primary focus of funding requirements should be based on long-term measures and long-term assumptions.

* Short-term measures of a plan's funded status should be monitored and taken into account in funding and disclosure decisions, but also must balance funding goals with the need to avoid forcing plan sponsors to choose between funding their plans and maintaining the viability of their businesses.

Financial Disclosure to Participants: More meaningful and more current disclosure is needed. Summary annual reports are not meaningful. Investors receive better and more current information than do plan participants.

* Plans should be required to provide participants early each year with a statement of the plan's funded status based on timely information currently available -- such as information on plans compiled for SFAS 87 disclosures.

* The new report should replace the summary annual report.

* As under current law, plans may provide participants with additional information.

Underfunded Plans: To prevent the occurrence of benefit accruals that are not likely to be funded within a reasonable period of time and to reduce the PBGC's exposure to such benefit accruals, special restrictions on benefit increases and payouts should be imposed on plans that are severely underfunded and likely to terminate. This will limit cost shifting from failed plans to ongoing plans through increased PBGC premiums.

* Restrictions should be imposed on a graded scale – the most severe restrictions reserved for the most underfunded plans.

* Restrictions imposed on benefit accruals or lump sum distributions must be workable and as minimally disruptive of business operations, workforce management goals, and participants' needs as possible, and not invite or lead to lawsuits against employers.

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