NATIONAL COORDINATING COMMITTEE FOR MULTIEMPLOYER PLANS

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Subcommittee on Health, Employment, Labor, and Pensions

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"Assessing the Challenges Facing Multiemployer Pension Plans"

Testimony of:

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Introduction

Chairman Roe, Ranking Member Andrews and Members of the Committee, it is an honor to speak with you today on this important topic. My name is Josh Shapiro. I am the Deputy Director of the National Coordinating Committee for Multiemployer Plans (the "NCCMP"). The NCCMP is a non-partisan, non-profit advocacy corporation created in 1974 under Section 501(c)(4) of the Internal Revenue Code. It is the only organization created for the exclusive purpose of representing the interests of multiemployer plans, their participants and sponsoring organizations. In addition to my role at the NCCMP, I am also a Fellow of the Society of Actuaries, a Member of the American Academy of Actuaries, and an Enrolled Actuary under ERISA. I serve on the American Academy of Actuaries Pension Committee, and on its Multiemployer Subcommittee.

The sponsors of multiemployer pension plans are predominately small businesses that operate in industries characterized by highly fluid employment patterns. For over 60 years multiemployer plans have made it possible for these companies to provide their employees with modest and reliable retirement income. Both the small size of the sponsoring employers and the mobility of their workforces make it impractical for them to achieve this objective with single-employer pension plans. For this reason, millions of middle class Americans have financial security in retirement that is entirely attributable to the existence of multiemployer pension plans. According to the 2011 PBGC Annual Report, there are currently approximately 1,450 multiemployer plans in the country covering over 10 million participants. While precise figures are difficult to obtain, the NCCMP has estimated that the aggregate assets held by these plans totals approximately $450 billion.

Multiemployer plans are the product of collective bargaining between one or more unions and at least two unrelated employers. The collective bargaining process establishes the rate at which employers will contribute to the plan, frequently expressed as a dollar amount per hour of work. The contributions go into a trust fund that is independent of either bargaining party. By law, the trustees of this fund consist of equal representation from both management and labor. With input from their professional advisors, the trustees determine the benefit provisions of the pension plan, oversee the investment of the assets, and administer the collection of contributions and the payment of benefits. As trustees, the representatives of both sides of the bargaining table have fiduciary responsibility to manage the plan for the sole and exclusive benefit of the plan participants.

While most often associated with the construction and trucking industries, multiemployer plans are pervasive throughout the economy including the agricultural; airline; automobile sales, service and distribution; building, office and professional services; chemical, paper and nuclear energy; entertainment; food production, distribution and retail sales; health care; hospitality; longshore; manufacturing; maritime; mining; retail, wholesale and department store; steel; and textile and apparel production industries. These plans provide coverage on a local, regional, or national basis, and cover populations that range from as small as a few hundred participants to as large as several hundred thousand participants.

The Experience of Multiemployer Plans in the 1990's

Since the establishment of ERISA's pre-funding requirements, multiemployer plans have typically been very well funded. This was especially true in the late 1990's when exceptionally strong stock market returns resulted in many plans having assets that were significantly larger than their liabilities. While on the surface this is a highly desirable result, it is ironic that this period actually set the stage for the challenges that the plans face today. To see why this is the case, it is first necessary understand how actuaries calculate the funding needs of multiemployer plans through the use of long-term assumptions and methods.

Long-term actuarial funding rests on the idea that the financial markets will experience periods of strong investment returns and periods of poor investment returns. The actuary determines the funding requirements using an assumed rate of return on plan assets that represents his or her best estimate of the long-term average, with the understanding that over short periods of time the assets may perform significantly better or worse than this average. The core idea is the notion that short-term fluctuations will tend to offset each other, and the plan can achieve stable long-term funding through the use of level and predictable contributions. In order for this funding approach to function properly, it is necessary for plans to maintain surplus positions during periods of unusually strong asset returns, as these surpluses will serve to offset the losses that the plans incur during periods of unusually poor returns.

During the late 1990's, very strong investment returns resulted in the majority of multiemployer plans having assets that exceeded their liabilities. While the long-term approach to funding dictates that plans need to preserve this overfunding to offset future investment losses, two unique features of multiemployer plans prevented them from remaining in a surplus position. The first of these features is the fact that contributions to multiemployer pension plans are specified in collective bargaining agreements. There is no simple mechanism for stopping or reducing these contributions when the plan is overfunded. The second unique feature of multiemployer plans is the fact that during the 1990's, contributions to an overfunded multiemployer pension plan were not tax deductible to the employers. In many cases, not only would contributions to these plans have been non-deductible, they would also trigger excise tax penalties.

The combination of these two features placed the trustees of multiemployer pension plans in a very difficult position. The employers were obligated by the collective bargaining agreements to contribute to the plans, but due to the overfunding of the plans, these contributions would not be tax deductible, and might trigger excise tax penalties. As a practical matter, the trustees had no choice but to raise the level of benefits that the plans provided so that the plan assets would no longer exceed the liabilities. Essentially, they were forced to spend the funding surpluses instead of being able to preserve them as insurance against a market downturn. The NCCMP has estimated that upwards of 70% of all multiemployer plans found themselves in this position leading up to the millennium. The Pension Protection Act of 2006 (PPA) addressed this shortcoming in the tax code, but unfortunately this change was too late to help most plans.

It is worth noting that the situation facing single-employer pension plans was very different. The most obvious difference was the fact that the sponsors of these plans had the option to simply stop contributing to the plans during periods of overfunding. Many plan sponsors took advantage of this option, and it was not uncommon for these companies to go ten or more years without making any contributions to the plans at all. At the same time, there was no need for these plans to raise their benefit levels to eliminate the overfunding, so many of them remained significantly overfunded year after year. Some observers have noted that single-employer plans have historically had higher funding levels than multiemployer plans. This observation is true, but most authors either miss, or choose to ignore, the fact that the ability of single-employer plans to effectively maintain a surplus position gave them an inherent funding advantage over multiemployer pension plans.

Market Turmoil of the 2000's

Having been unable to maintain a surplus position during the late 1990's, multiemployer pension plans were extremely vulnerable to the market turmoil that characterized the decade between 2000 and 2010. Despite the downturn that occurred in the years 2000 to 2003, by the beginning of 2008 multiemployer plans were very much back on track. NCCMP survey data indicates that at the beginning of that year, the average plan was approximately 90% funded. The Pension Protection Act of 2006 (PPA) established criteria for determining when a multiemployer plan should be considered in 'endangered status' or 'critical status'. NCCMP survey data shows that at the beginning of 2008, only 9% of plans were considered to be 'critical', with an additional 15% classified as 'endangered'.

The 2008 financial market crash and ensuing recession had a profound impact on the funding position of multiemployer plans. The S&P 500 Index lost 37% that year, and the average multiemployer plan experienced a decline of approximately 30% in its funded level (determined using the market value of assets). For many plans with funding ratios of 90% or better prior to the crash, the level of contributions needed to responsibly fund the liabilities more than tripled. This situation placed enormous burdens on companies that were already contending with a historically difficult economic climate in the years following the 2008 crisis. The recession also presented a separate challenge for he plans themselves, as they depend on employment levels to generate contribution income. As an analogy, the 2008 crash gave the plans a hole from which they need to dig out, and the subsequent recession substantially reduced the size of their shovel.

It is critical to note that the funding challenges currently facing multiemployer plans are not the result of reckless investing, aggressive assumptions, or unreasonably large benefits. NCCMP survey data clearly documents this conclusion. This data indicated that at the beginning of 2008, the average multiemployer plan held approximately 57% of its assets in equities, 27% in bonds, 6% in real estate, and the remaining 10% spread across cash, hedge funds, private equity, and other investments. This asset mix is in line with the portfolios of pension funds in other sectors, and is also consistent with the strategy that investment professionals recommend to individuals who need to manage their own retirement savings through defined contribution plans.

Regarding actuarial assumptions, the vast majority of multiemployer pension plans budget for average returns of 7.5% or less on their investments. This figure represents a reasonable estimate of the asset returns that are attainable to investors with very long-term time horizons. NCCMP survey data indicates that the median benefit that a multiemployer plan pays to a retiree is approximately $900 per month, which is just under $11,000 per year. As most retirees have been receiving their benefits for many years, a better measure of the benefits that the plans are currently promising is to look at the median amount paid to a recent retiree. This figure is approximately $1,400 per month, or just under $17,000 per year. By any measure, these are modest retirement benefits that, when combined with Social Security and personal savings, are just enough to allow retired participants to have a decent standard of living.

The Road to Recovery

When a multiemployer plan encounters adverse experience, the trustees and bargaining parties have two main tools at their disposal to improve the funded position of the plan. The first tool is to allocate additional contributions to the plan. When this tool is used, it has a direct effect on both the employees and the employers. For the employees, it serves to reduce their overall compensation, since absent the funding challenges of the pension plan, these dollars would have been available for other purposes. In fact, in many severely troubled plans employees have accepted reductions in their paycheck wages in order to allocate more money to the pension plan. For the employers the additional contributions make it more difficult for them to compete in the market place, often against competitors that have not chosen to provide comparable retirement benefits to their employees. NCCMP survey data indicates that more than 70% of multiemployer plans have responded to the 2008 funding crisis with increased contributions.

The second tool available for the purpose of improving the funded position of a multiemployer pension plan is to reduce the rate of future benefit accrual. This action has minimal immediate effect on the plan as it does not affect benefits that participants have already earned. What it does do is allow a larger portion of the ongoing contribution income to pay for the funding shortfall, as a lesser portion of these contributions is required to cover the cost of participants' benefit growth. In contrast to the first tool that impacts both the employees and the employers, reducing the rate of benefit accrual only has a direct impact on the employees. NCCMP survey data indicates that approximately 40% of multiemployer plans have responded to their funding challenges by reducing the rate of benefit accrual.

The actions that multiemployer boards of trustees and sponsoring employers have taken in response to the financial crisis have been difficult for all stakeholders. However, these actions have not only been necessary, they have been effective. While NCCMP survey data indicates that only 20% of plans were in the PPA ‘green zone’ immediately following the 2008 crash, current data indicates that this figure now exceeds 60%. An occasional, and particularly ill informed, criticism of multiemployer plans is that they have ignored their problems. Regardless of how someone feels about multiemployer pension plans, any thorough analysis of their recent history will demonstrate the commitment that both the employees and employers have to the plans, and the sacrifices they have made to support them.

Despite the efforts of the sponsors to take the measures necessary for recovery, a small number of plans have suffered more damage than they will be able to endure. Primarily these plans come from industries in which economic shifts have greatly hindered their ability to raise the necessary contribution income. In particular, there are two specific very large plans that have suffered from the unintended consequences of unrelated public policy decisions. In one of these plans, the deregulation of the trucking industry in 1980 resulted in the decline and demise of virtually all of the major contributing commercial carriers. In the other plan, the Clean Air Act caused the cessation of a large portion of the bituminous coal mining industry that previously contributed to the plan, resulting in an active employee population that is a small fraction of the previous number. In both instances, the plans had managed to remain well funded until the unprecedented market collapse imposed irrevocable harm on the plans’ investments. While these two plans represent major challenges to the multiemployer community, and they are the subject of frequent media attention, their unique circumstances are not representative of the vast majority of multiemployer plans.

NCCMP Retirement Security Review Commission

The multiemployer funding provisions of the Pension Protection Act of 2006 (PPA) will sunset at the end of 2014. The challenges currently facing multiemployer plans make it clear that in order to survive and grow in the future, the system requires a greater degree of flexibility than is currently available. We have welcomed the interest shown by your Committee staff and that of the other Committees of jurisdiction, as well as the regulatory agencies in learning how PPA could be modified to better meet the needs of plan participants, sponsors and the plans themselves. In the course of reviewing proposals for modifications, we have come to the conclusion that now is an appropriate time to consider taking a more fundamental assessment of the rules governing the multiemployer defined benefit system.

In order to ensure that the interests of all stakeholders are reflected in this evaluation, the NCCMP has convened a “Retirement Security Review Commission” comprised of representatives from over 40 labor and management groups from the industries which rely on multiemployer plans to provide retirement security to their workers. The group began its deliberations in August of 2011 and meets monthly to evaluate their collective experience with current laws and regulations and develop ideas for reform and improvement.

The group has identified the following key objectives:

- Ensure that any proposed changes to the law or regulations will allow the plans to continue to provide regular and reliable retirement income to participants.

- Reduce the financial risks to employers so that these risks do not encourage companies to leave the system or prevent new companies from joining the system.

The Commission has established an ambitious time table for its deliberations with a target of developing legislative recommendations later this summer. We look forward to keeping your Committee staff apprised of our progress, and to discussing our recommendations when they are available. We are confident that labor, management, and government will be able to work together to achieve the necessary enhancements that will enable multiemployer plans to survive and continue to provide affordable, reliable and secure retirement income to future generations of Americans.