



Testimony of
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before the
HOUSE COMMITTEE ON EDUCATION AND THE WORKFORCE
SUBCOMMITTEE ON HEALTH, EMPLOYMENT, LABOR, AND PENSIONS
Hearing
"Financial Challenges Facing the Pension Benefit Guaranty Corporation:
Implications for Pension Plans, Workers, and Retirees"
November 29, 2017

Chairman Walberg, Ranking Member Sablan, Members of the Subcommittee.

Thank you for the opportunity to appear before you today to discuss the Pension Benefit Guaranty Corporation (PBGC) and the challenges it faces in protecting pensions of American workers.

PROTECTING PENSIONS

Every American worker should have access to a secure retirement. A vital part of that security for nearly 40 million private-sector workers, retirees, and beneficiaries comes from traditional defined benefit pension plans. PBGC's mission is to protect the lifetime retirement income that comes from those plans when employers can no longer afford them. Without PBGC, more than two million participants and beneficiaries in about 5,000 plans that have failed since PBGC was established might have lost the pensions they earned for years of work.

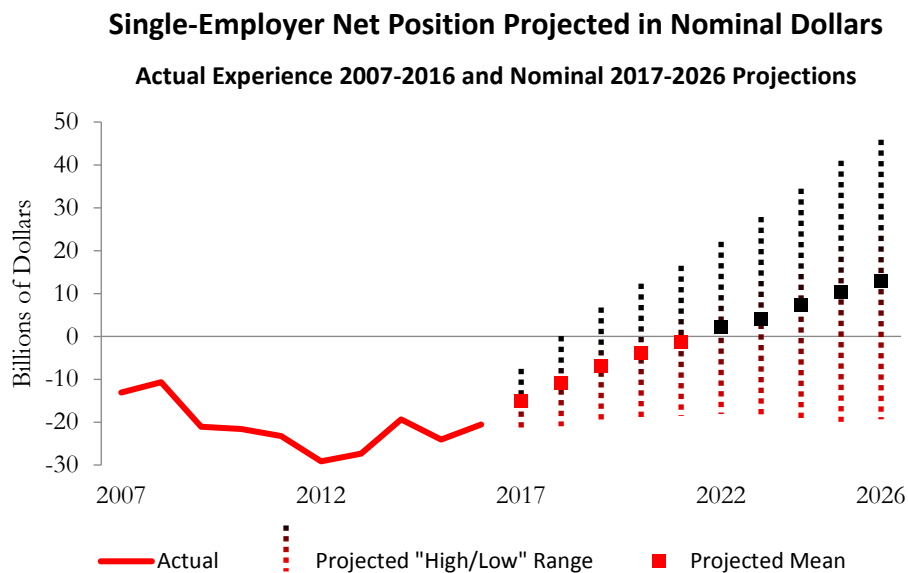
Congress established PBGC as part of the Employee Retirement Income Security Act of 1974 (ERISA). By law, PBGC is self-financed and receives no taxpayer money. PBGC is administered by a Director. PBGC has a three-member Board of Directors consisting of the Secretary of Labor, who is Board Chair, and the Secretaries of the Treasury and Commerce.

PBGC operates two separate insurance programs: one for single-employer plans and one for multiemployer plans (collectively bargained plans with more than one employer). While each program is designed to protect participants' pension benefits when plans fail, they differ significantly in the level of benefits guaranteed, how the guarantee is provided, the event that triggers payment of the guarantee, and premiums paid by insured plans. By law, the two programs are financially separate. Assets of one program may not be used to pay obligations of the other.

Both programs have been in a deficit position for fifteen years or longer, meaning that, for each of our two insurance programs, assets are less than liabilities. While the financial condition of the Single-Employer Program has been improving, the financial condition of the Multiemployer Program is dire and without action will be worse.

As of September 30, 2017, the Single-Employer Program had liabilities of \$117.1 billion and assets of \$106.2 billion, resulting in a \$10.9 billion deficit, down from a \$20.6 billion deficit at the end of FY 2016. Continued improvement in the Single-Employer Program is projected but not a certainty. PBGC's FY 2016 Projections Report shows that the Single-Employer Program will no longer be in a deficit position by the year 2022 (see Figure 1 below).¹

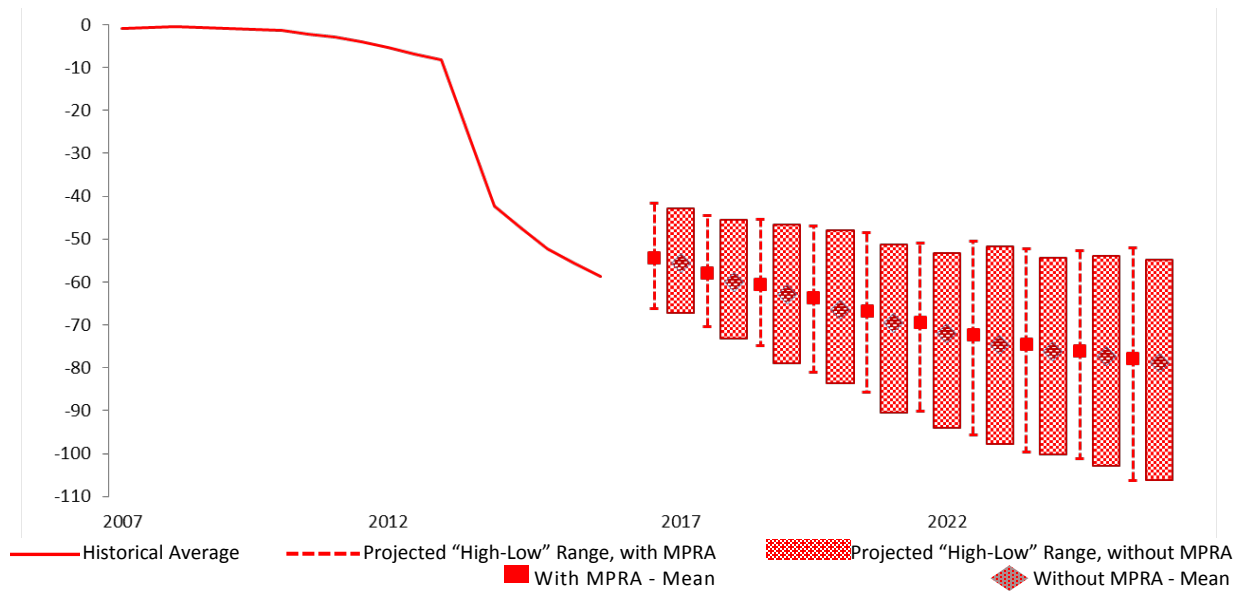
Figure 1.



In sharp contrast, the Multiemployer Program had liabilities of \$67.3 billion and assets of only \$2.3 billion, resulting in a \$65.1 billion deficit. PBGC's FY 2016 Projections Report shows a projected 2026 mean present value deficit of about \$78 billion (in nominal dollars) in the Multiemployer Program, even assuming that some plans use benefit suspensions and partitions under the Multiemployer Pension Reform Act of 2014 (MPRA) to avoid insolvency (see Figure 2 below).

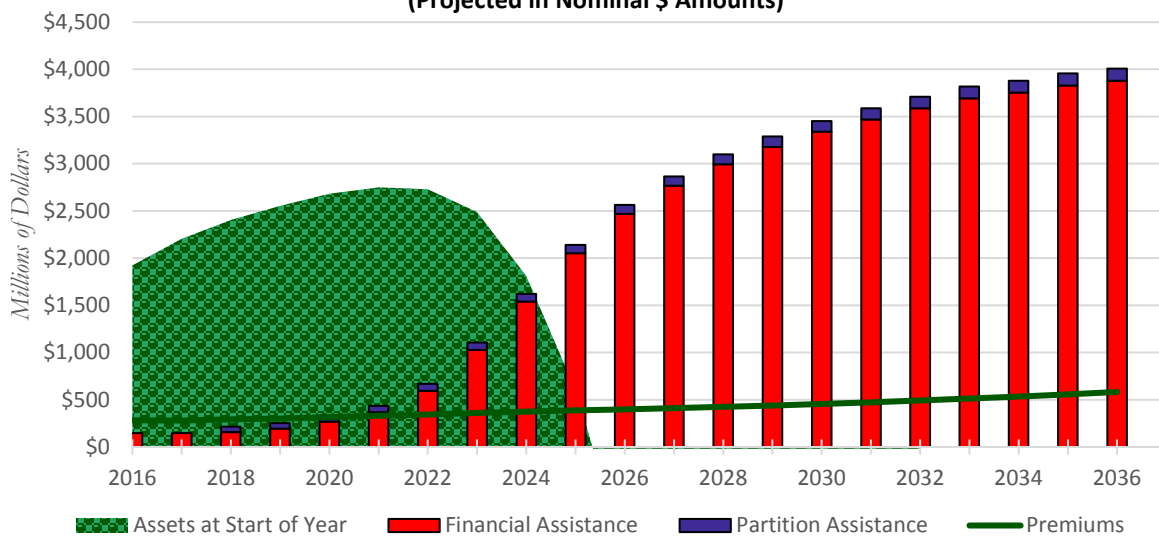
¹ PBGC uses stochastic modeling that produces a probability distribution of potential outcomes for the future financial condition of PBGC's two insurance programs. The FY 2016 Projections Report continues to show a wide range of potential outcomes.

Figure 2.
Multiemployer Program Net Position
 Reflecting Assumed MPRA Suspensions / Partitions
 Historical Experience 2007-2016 and Nominal 2017-2016 Projections



The assets and income of PBGC's Multiemployer Program are only a small fraction of the amounts PBGC will need to support the guaranteed benefits of participants in plans expected to become insolvent during the next decade. Projections show that the Program is likely to become insolvent by the end of 2025, absent changes in law (see Figure 3 below).

Figure 3.
PBGC Assets, Average Assistance Payments and Premiums by Fiscal Year
 Reflecting Assumed MPRA Suspensions / Partitions
 (Projected in Nominal \$ Amounts)



As insolvency of the insurance program grows closer, the changes required to prevent insolvency become more disruptive and painful for participants, plans, and employers.

Most of my testimony today will be about the Multiemployer Program and the urgent need to fix its problems.

But let me talk first about the Single-Employer Program.

SINGLE-EMPLOYER PROGRAM

The Single-Employer Program protects about 30 million workers and retirees in about 22,500 ongoing pension plans. The program is funded by premiums, investment income, assets we take over when a plan fails, and recoveries from employers who sponsored these failed plans.

When an employer can no longer maintain its pension plan—often in the case of company bankruptcy or business failure—the plan is terminated and PBGC steps in and becomes the trustee of the plan. PBGC pays benefits promised under the plan subject to statutory limits. In some cases, plan assets and PBGC recoveries of unpaid contributions and unfunded benefits from plan sponsors enable PBGC to pay more than the statutory guarantee. While PBGC is reviewing plan records, valuing plan assets, and determining final benefit amounts—often a complex and lengthy process, especially in large plans—PBGC pays estimated benefit amounts.

In FY 2017, PBGC paid \$5.7 billion in benefits to 840,000 retirees and beneficiaries in nearly 4,900 plans. PBGC will pay benefits to an additional 552,000 people in these plans when they retire.

Excellent customer service is a top priority at PBGC. In FY 2017, PBGC received a retiree customer satisfaction score of 91, which is among the best in public and private sectors, according to the American Customer Satisfaction Index.

Preserving Plans

We work hard to keep plans ongoing. An ongoing plan generally is the best outcome for everyone—

- Workers continue to earn benefits (if the plan is not “frozen”);
- Plan benefits are preserved, as no one suffers a benefit reduction as a result of guarantee limitations;
- The employer is not faced with a sudden claim for plan underfunding;
- The insurance program does not incur an avoidable claim, which protects other premium payers from future premium increases; and
- Employers are able to maintain their promises to employees.

In FY 2017, PBGC helped to protect more than 26,700 people by taking action in bankruptcy cases to encourage companies to keep their plans when they emerged from bankruptcy.

Through our Early Warning and Risk Mitigation Program, we worked closely with sponsors to create satisfactory arrangements to safeguard participant benefits. These agreements provided almost \$600 million in financial protection for more than 240,000 people in plans put at risk by corporate transactions. These agreements also avoid placing an unnecessary burden on all employers who pay PBGC premiums.

Trends

Defined benefit pensions have long been and remain an important component of retirement security for a significant number of workers and retirees. But as the GAO noted in its recent report on Retirement Security², beginning in the mid-1980's sponsors of single-employer defined benefit plans have been moving away from these plans. That trend is accelerating as companies seek to limit their exposure to risk and contribution volatility by freezing plans or transferring risk through annuity purchases and lump sum payout options.

We at PBGC are doing what we can to help employers keep their defined benefit plans. We have increased our outreach to the pension community through more and improved communications and opportunities to provide us with input. We want plan sponsors and plan practitioners to know that we are serious about understanding and addressing their concerns.

In FY 2017, we cut in half the penalty rates for late payment of premiums for all plans and waived most of the penalty for plans that meet a standard for good compliance with premium requirements. We also upgraded our online premium filing application to make filing easier and quicker. These upgrades resulted in our premium payers giving us a customer satisfaction score of 85 in FY 2017, an all-time high that exceeds PBGC's target of 79.

On October 16, 2017, PBGC announced the creation of a Pilot Mediation Project in the Single-Employer Program that will offer voluntary mediation to plan sponsors to facilitate resolution of negotiations in certain Plan Termination Liability Collection and Early Warning and Risk Mitigation Program cases. The Pilot Mediation Project will allow parties to resolve cases with the assistance of a skilled, neutral and independent dispute resolution professional.

EXTENDING THE MISSING PARTICIPANTS PROGRAM TO MORE TYPES OF TERMINATING PLANS

Another innovation coming soon is the expansion of PBGC's Missing Participants Program to enable most terminating defined contribution plans to transfer the benefits of missing participants to PBGC or to inform PBGC about other arrangements for distributing their benefits. Through PBGC's search efforts and its centralized online searchable database, the expanded Missing Participants Program will help participants find and receive the benefits being held for them. The expanded program also will cover terminating small professional service pension plans and multiemployer plans. PBGC expects the expanded program to be operational in 2018 after publication of a final rule.

² The Nation's Retirement System: A Comprehensive Re-evaluation Is Needed to Better Promote Future Retirement Security. [GAO-18-111SP](#); Published: Oct 18, 2017. Publicly Released: Oct 18, 2017.

MULTIEMPLOYER PROGRAM

A multiemployer plan is a pension plan created through a collective bargaining agreement between employers and a union. The employers are usually in the same or related industries. Multiemployer plans provide benefits for people in industries such as transportation, construction, mining and hospitality.

The Multiemployer Program protects over 10 million workers and retirees in about 1,400 ongoing multiemployer plans. Multiemployer plans overall are less well funded than single-employer plans. Most multiemployer plans covering a majority of multiemployer participants are not at risk of running out of money. But a significant minority of multiemployer plans, some very large, and covering one million participants, are seriously underfunded and project they will run out of money within in the next 20 years.

PBGC's Multiemployer Program provides financial assistance to multiemployer plans that have run out of money so that they can pay benefits at PBGC guaranteed levels.³ The program is funded by premiums paid by the plans. Our financial assistance is technically a loan to the insolvent plan. But because insolvent plans are in such dire financial condition, financial assistance loans are almost never repaid.

Causes of Multiemployer Plan Underfunding

Many factors – financial, economic, and demographic – contributed to the financial distress of some multiemployer plans.

Before the decade of the 2000s, defined benefit plans, including multiemployer plans, earned historically high rates of return, which kept plans well-funded without large employer contributions. High investment returns financed benefit improvements, such as increased benefit accrual rates, past service credits, new or increased early retirement subsidies, and disability pensions.⁴ These new obligations compounded the plans' liabilities during the 1990s.

The significant market losses in the early 2000s and especially in the 2008 market crisis and great recession took a huge toll. Average funded ratios (market value of assets divided by liabilities discounted using a standardized PBGC interest factor) exceeded 90% in the 1990s, then dropped to the mid-60% range in the mid-2000s, and fell below 50% after the 2008 market crisis.

Most plans were able to recover but a significant number were not, including some very large plans covering thousands of participants and in a few cases hundreds of thousands.

Factors such as decline in unionized employment, competitive pressures from non-unionized businesses, and decline in demand for products or services, caused some companies to go out of business. They left behind the unfunded benefits of their inactive and retired workers (sometimes referred to as orphan liabilities). Today, the ratio of active to inactive participants is at its lowest point ever: among multiemployer plans in the aggregate, fewer than four out of

³ Financial assistance also covers reasonable administrative expenses.

⁴ Because of maximum deductible limits, some plans increased benefits during this period to avoid losing deductible treatment of employer contributions, which also contributed to longer-term costs. These limits were raised in the Pension Protection Act of 2006.

every ten covered participants is actively employed by a participating employer. In addition, downsized companies that remained in business contributed on fewer hours worked. As underfunding in these plans deepens, remaining employers are faced with a difficult choice: higher contributions if they stay; higher withdrawal liability if they leave. And if they do leave, the plan will be at greater risk of failure.

Severity of the Problem

PBGC's Financial Statements reflect the serious underfunding in these multiemployer plans and our Projections Report shows how this underfunding is likely to result over time in a growing deficit and more important, the inability of the Multiemployer Program to provide the financial assistance that failed plans need to pay guaranteed benefits.

In FY 2017, PBGC paid \$141 million in financial assistance to 72 multiemployer pension plans, covering the benefits of over 63,000 retirees with an additional 30,000 people entitled to benefits once they retire. Seven of the 72 plans became insolvent during FY 2017. In the coming years, the demand for financial assistance from PBGC will increase as more and larger multiemployer plans run out of money and need help to provide benefits at the guarantee level set by law.

As of September 30, 2017, the Multiemployer Program had assets of \$2.3 billion to cover \$67.3 billion in liabilities in 187 plans. The liabilities consist of:

- \$2.7 billion for the 72 plans currently receiving financial assistance
- \$2.0 billion for 68 plans that have terminated but have not yet started receiving financial assistance payments from PBGC. Terminated multiemployer plans no longer have employers making regular contributions for covered work, though some plans continue to receive withdrawal liability payments from withdrawn employers
- \$62.7 billion for 47 plans that are ongoing (i.e., have not terminated), but PBGC expects they will exhaust plan assets and need financial assistance within 10 years.⁵

The last two categories—terminated plans and ongoing plans expected to need financial assistance within 10 years—are classified as “probable” obligations of the Multiemployer Program.

The \$67.3 billion in Multiemployer Program liability is an increase from \$61.0 billion in FY 2016. In addition to the \$67.3 billion booked as a liability in our financial statements, there is \$14 billion in underfunding that is not reflected in our financial statements in ongoing multiemployer plans projected to become insolvent in the next 10 to 20 years; these plans are classified as “reasonably possible” future obligations.

As noted earlier, our most recent projections show that, absent a change in law, the mean present value 2026 deficit is about \$78 billion (in nominal dollars), and Multiemployer Program assets are likely to be exhausted in 2025.⁶

⁵ The liability for ongoing plans includes a small probable bulk reserve of \$1.1 billion.

⁶ PBGC FY 2016 Projections Report.

Consequences of Multiemployer Program Insolvency

When Multiemployer Program assets are exhausted, the only money available to provide financial assistance for benefit payments will be incoming multiemployer premiums. Multiemployer premium income in FY 2017 was under \$300 million, and the annual premium rate, \$28 per participant for 2017 and 2018 plan years, will increase only by indexing. Premium revenue will be too low to provide the annual financial assistance required for insolvent plans. As a result, funds in the Multiemployer Program will represent only a small fraction of current guarantee levels.

Further, under ERISA, multiemployer guarantees are already much lower than single-employer guarantees. For example, the maximum guaranteed benefit for a retiree with 30 years of service is \$12,870 annually; the multiemployer guarantee has not increased since 2001 and is not indexed for inflation. In contrast the maximum guaranteed benefit for a retiree in a single-employer plan is \$64,432 annually, reduced for people younger than age 65⁷ and for the value of any survivor benefits; the single-employer guarantee is indexed for inflation.

PPA and MPRA

Congress enacted two pieces of legislation to address underfunding in multiemployer plans: The Pension Protection Act of 2006 (PPA) and the Multiemployer Pension Reform Act of 2014 (MPRA).

The Pension Protection Act of 2006 categorized multiemployer plans based on funded status, compliance with minimum funding standards, and time until likely insolvency. Plans with severe funding and liquidity issues were categorized as “critical status” plans (commonly referred to as “red zone” plans). Generally, these are plans that are likely unable to meet minimum funding requirements or are likely to become insolvent in the near term.

Under PPA, critical status plans must establish a Rehabilitation Plan detailing how they intend to emerge from critical status (generally within 10-13 years, through actions such as increasing contributions and reducing future accruals or adjustable benefits). If they are not projected to emerge during the rehabilitation period after exhausting all reasonable measures, they must develop an alternative scenario that allows them to emerge at a later time or to otherwise forestall possible insolvency.

The Multiemployer Pension Reform Act of 2014 defined a subcategory of critical status plans that are “critical and declining.” These are critical status plans whose actuaries project that plan insolvency will occur within 15 years (or in certain situations, within 20 years).

MPRA gives critical and declining plans additional options to address the risk of insolvency, but the use of these options presents difficult choices for plan sponsors and participants. Under MPRA, critical and declining plans may take steps to improve long-term solvency by permanently reducing benefit promises to participants via benefit suspensions if they meet certain requirements, including application to and approval by the Department of the Treasury.

MPRA also changes PBGC’s ability to provide early financial assistance to plans, either by assuming part of the plan’s liabilities via a plan partition or by providing facilitated merger assistance. To receive partition assistance, the plan must take all reasonable measures to avoid

⁷ The maximum guarantee is increased for ages above 65.

insolvency including the maximum benefit suspensions, if applicable. Mergers can stabilize or increase the base of contributing employers, combine plans' assets for more efficient investing, and reduce plans' administrative costs. Under MPRA, PBGC is authorized to help plans merge with other multiemployer plans. Plans may request technical assistance, and critical and declining plans may also apply for financial assistance to facilitate a merger, if necessary to avoid plan insolvency. PBGC is working on a final rule that would provide guidance on the process of requesting a facilitated merger.

The new options provided by MPRA are also expected to reduce PBGC's liability. A partition, or any facilitated merger, must reduce PBGC's long-term loss and cannot impair its ability to provide financial assistance to meet existing obligations to other plans.

PPA and MPRA can help some critical and declining plans but cannot help all of them. In some cases, underfunding is so large relative to future cash inflows that benefit suspensions and partition cannot keep the plan solvent long-term.

The Road Carriers Local 707 Pension Fund, which is based in Hempstead, New York and covers nearly 5,000 participants, illustrates the problem. In 2016, the 707 Fund became unable to pay full benefits at the levels promised under the plan, and reduced retirees' benefits to levels that were supportable by available plan assets. The Fund applied for MPRA benefit suspensions and a PBGC partition in order to preserve benefit payments above PBGC guarantee levels. But projected future contributions and other income were insufficient to avoid insolvency, even with the maximum benefit reductions allowed under MPRA and a PBGC partition. The plan became insolvent early in 2017, and the agency began providing financial assistance to the plan to cover benefits at PBGC guaranteed levels.⁸ As a result of the plan's insolvency, nearly one-half of all participants had their benefits reduced by more than 50 percent.

Where MPRA is a viable option, the degree to which plans will attempt to extend solvency through benefit reductions and requests for early financial assistance requests remains unknown. As of the close of FY 2017, fifteen troubled plans had made an application for suspension, with three also seeking a partition from PBGC to remain solvent. To date, only one combined application for suspension and partition, and three suspension-only applications, had received all the required approvals.⁹

In modelling projected insolvency dates and deficits for the Multiemployer Program, PBGC looked at scenarios where some plans use MPRA benefit suspensions or early financial assistance and where no plans used such MPRA tools. The mean date for Multiemployer Program insolvency was 2025 in both scenarios. The mean 2026 deficit in nominal dollars differed only slightly by scenario—\$77.8 billion with MPRA and \$78.8 without use of MPRA.

⁸ News Release: PBGC Provides Financial Assistance to Road Carriers Local 707 Pension Fund - Participants' Benefits Payments Cut to PBGC Guaranteed Levels. <https://www.pbgc.gov/news/press/releases/pr17-02>

⁹ Ironworkers Local 17 Pension Fund received final authorization on January 27, 2017 <https://www.treasury.gov/services/Responses2/Iron-Workers-Local-17-Final-Approval-Letter.pdf>. As it occurred after September 30, 2016 it is not reflected in the report scenario which shows no future suspensions.

Helping Plans Avoid Plan Insolvency

We work with troubled multiemployer plans and their sponsors who come to us seeking to prevent plan insolvency. We provide advice and assist them in whatever way we can.

This year we approved the first plan partition under the Multiemployer Pension Reform Act of 2014 (MPRA) for the United Furniture Workers Pension Plan A. Under partition, early financial assistance from PBGC before the plan becomes insolvent, along with required benefit reductions, will help the plan to avoid insolvency and pay benefits above the guarantee level to nearly 10,000 participants over the long term.

But the tools PBGC has to address the multiemployer crisis are very limited. We have been working with stakeholders and policy makers to find new ideas for shoring up the program.

Legislation is needed to address the looming insolvency of PBGC's Multiemployer Program and again make the PBGC guarantee something American workers and retirees, and their families, can count on. A number of proposals have been put forward. Some are designed to help plans avoid insolvency and thus help PBGC indirectly. Others are designed to help PBGC avoid insolvency.

The President's FY 2018 Budget included a proposal to shore up the PBGC's Multiemployer Program. The Budget proposes adding a variable-rate premium on unfunded benefits, similar to the Single-Employer Program, with provision for waiver to avoid accelerating insolvency in the most troubled plans. The proposal also includes an exit premium on companies that withdraw from multiemployer plans. The proposal is estimated to raise an additional \$16 billion over the ten-year budget window.

CONCLUSION

While the Single-Employer Program is improving, the Multiemployer Program is headed toward insolvency. It is more likely than not that the program will run out of money in 2025.

The longer the delay in making the changes needed to improve the solvency of the Multiemployer Program, the more disruptive and painful those changes will be for participants, plans, and employers.

If the PBGC Multiemployer Program is allowed to become insolvent, the only money available to provide guaranteed benefits will be incoming premiums. Only a small fraction of the current, very modest guarantee will then be funded. The result will be catastrophic for many people—current and former workers, retirees, beneficiaries, and their families.

I appreciate the leadership that the members of this Subcommittee have provided in calling attention to the challenges faced by multiemployer plans and the PBGC Multiemployer Program. I look forward to continuing to work with you to ensure that PBGC's guarantee is one that workers and retirees can count on in the future.

I am happy to answer any questions.