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May 28, 2024

The Honorable Bernie Sanders, Chair
Committee on Health, Education, Labor and Pension
428 Senate Dirksen Office Building
Washington, DC 20510

RE: Request for Information on Retirement Security for All and Defined Benefit Plan Improvements

Dear Chair Sanders:

Thank you for the opportunity to provide feedback on the Majority Staff Report dated February 28, 2024 and your subsequent request for information (RFI) regarding the proposed Retirement Security for All legislation and ways in which to improve the defined benefit pension plan system. Our input and comments are below.

Defined Contribution Plan RFI

The Retirement Security for All proposal would require businesses that have been operating for two years or more to offer an automatic enrollment payroll deduction plan with lifetime income options to all employees (to include full, part-time, and 1099 workers). The requirement would be satisfied if a business:

- Offers a defined benefit pension plan to its workforce (not just to highly compensated corporate officers);
- Offers a qualified defined contribution retirement plan with automatic enrollment, automatic reenrollment, and automatic escalation; and a monthly income option (to include managed payout, annuities, and/or a Social Security bridge);
- Offers a state facilitated retirement plan with the above features; or
- Offers access to the federally facilitated pension plan.

Under this proposal for the federally facilitated pension plan, the Federal government would set up a pension plan via a public-private partnership for use by employers that choose to offer it instead of sponsoring their own plan. No details were provided on the design, cost, or administration of this plan.

Defined Contribution Plan Proposal Response

According to the Bureau of Labor Statistics, "[i]n March 2023, 73 percent of civilian workers had access to retirement benefits, with 56 percent of workers participating in these plans. The take-up rate (the percent of workers with access to an employer-sponsored benefit who choose to participate in the benefit) for retirement benefits was 77 percent in March."[1] This is a significant change in coverage compared to 50 years ago when the Employee Retirement Income Security Act (ERISA) was enacted. In 1975, one year after ERISA was enacted, only 46.2 of all private industry workers were covered by retirement plans.[2] However, of that 46.2 percent, it was highly likely that a number of those covered never received any benefits because of short tenure and vesting schedules as long as 10 years. According to the Employee Benefits Research Institute, the vesting rate (namely, the percentage of the entire population with at least some entitlement to some employer contribution) in 1979 was only 24%. For those who actually participated in a plan, or the participant vesting rate, it was 52%, meaning that only half of those covered by a plan received a benefit. As GAO noted in its report:

> some have noted that the growth of DC plans since 1974 may have resulted in a greater share of private-sector workers receiving income from retirement plans. The reasons may include (1) lengthy vesting provisions that may have prevented some individuals in DB plans from receiving benefits and (2) the overall lower costs of DC plans, which may have resulted in more employers offering these plans.[3]

There have been many positive changes to ERISA and the Internal Revenue Code (Code) that have increased coverage, participation, and benefits in the employer-sponsored system. The Retirement Equity Act of 1984 strengthened participation rules by lowering the minimum age that a plan may require for enrollment from age 25 to age 21 and lowering the minimum age for vesting service from age 22 to age 18. The Tax Reform Act of 1986 changed the minimum vesting requirements to either one of the following options: five-year cliff or graded, under which participants are 20 percent vested after three years, with an additional 20 percent each subsequent year. The Economic Growth and Tax Relief Reconciliation Act changed vesting on matching contributions: the 5-year cliff or 7-year graded was replaced by a 3-year cliff or 6-year graded vesting. The Pension Protection Act (PPA) of 2006 allowed for automatic enrollment in Code Section 401(k) plan features.

More recently, both the Setting Every Community Up for Retirement Enhancement (SECURE) and The SECURE 2.0 Act (SECURE 2.0) included provisions that would expand coverage to part-time employees, expand coverage through Pool Employer Plans, encourage small employers to establish plans by making tax credits available, and enhance retirement savings for lower income individuals with the Savers' Match.

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[1] "TED: The Economic Daily", September 29, 2023 available at https://www.bls.gov/opub/ted/2023/73-percent-of-civilian-workers-had-access-to-retirement-benefits-in-2023.htm.

[2] "EXPANDING PRIVATE RETIREMENT PLAN COVERAGE AND BENEFITS: PROPOSALS BEFORE THE NINETYFIFTH AND NINETY-SIXTH CONGRESSES", Peter H. Turza, Duke Law Journal, Vol. 1979:615 available at https://scholarship.law.duke.edu/cgi/viewcontent.cgi?article=2705&context=dlj.

[3] "A Visual Depiction of the Shift from Defined Benefit (DB) to Defined Contribution (DC) Pension Plans in the Private Sector", Dec. 27, 2021 available at https://crsreports.congress.gov/product/pdf/IF/IF12007.

Recently, there has been increased interest from the private sector in providing retirement solutions for small business, which is where the retirement coverage gap exists. Experts predict that by 2026, 86 percent of employers with fewer than 100 employees will offer defined contribution plans, up from 46 percent in 2022.[4] Many of the provisions in SECURE and SECURE 2.0 are likely to be attributable to this expansion. Furthermore, more and more service providers are focusing on this market by creating programs specifically targeted at smaller employers. For example, WTW, Morningstar and Voya have all recently launched products specifically for the small market, and JP Morgan has partnered with Vestwell to provide increased support for its small-business savings offering.[5] In addition, numerous fintech providers are providing services to the small and micro-markets, such as Penelope and Finhabits.[6]

Given the positive changes in SECURE and SECURE 2.0 and the current marketplace that on its own is expanding coverage in the small market, new legislation creating a federal system is unnecessary. Instead, the focus should be on improving the current system to encourage employers to offer coverage. For example, the Saver's Match in SECURE 2.0 could be simplified so that more employers are willing to accept the match. Also, the pension linked emergency savings account provisions of SECURE 2.0 could be simplified to encourage adoption. Congress also could encourage the Department of Labor to issue regulations on SECURE Section 204 that would protect employers who offer lifetime income options under their 401(k) plan. We look forward to working with you on these and other ways to improve the current system, including streamlining reporting and disclosures requirements.

Defined Benefit Plan Improvement Response

There are many outside factors that may make it difficult for certain employers to bring back or establish traditional defined benefit plans.[7] However, there are numerous factors

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[4] "Experts Predict Major Growth in Retirement Coverage, Benefits", Natalie Lin, Mar. 23, 2023 available at https://www.planadviser.com/experts-predict-major-growth-retirement-coverage-benefits/#:~:text=Experts%20predict%20massive%20growth%20in,according%20to%20new%20industry%20research.

[5] "Changing Dynamics of US Small Plan Retirement Market", Rashabh Hingar and Pankaj Aggarwal available at https://www.evalueserve.com/blog/changing-dynamics-of-us-small-plan-retirement-market/.

[6] See "Retirement Fintech for SMBS Raises $2.1 M", Mar. 17, 2022 available at https://workweek.com/2022/03/17/retirement-fintech-for-smbs-raises-2-1m/; "Latino-Owned Businesses May Be Poised for 401(k) Plan Growth", Alex Ortolani, Mar. 29, 2023 available at https://www.planadviser.com/latino-owned-businesses-may-poised-401k-plan-growth/.

[7] We are not taking a position on whether a defined benefit plan is better or worse than a defined contribution plan because whether a plan is beneficial for an employee depends on whether the employee is a long or short tenured employee. In addition, certain employers may not be in a position to sponsor a defined benefit program because of the longevity and other risks. As such, we hope that Congress will look at ways to make both types of plans easier to sponsor so that an employee may make the choice of plan based on employee demographics and the employer's abilities. See "Suddenly Everyone's Talking about Defined Benefit Plans", Alice Munnell, Nov. 21, 2023 available at https://crr.bc.edu/suddenly-everyones-talking-about-defined-benefit-plans/.

within Congress' control that could ease the burden of maintaining a traditional defined benefit plan, creating or facilitating new designs, or allowing the use of funds to more equitably distribute funds accumulated within a traditional defined benefit plan.

PBGC Premiums

Over the years, Congress has focused on how to prevent the PBGC from having to pay benefits, which is the only purpose of the PBGC, through increased premiums and forced funding. This focus has helped stabilize the PBGC,[8] but it also has had the unintended consequence of forcing employers to terminate their plans, which is contrary to PBGC's mission to "encourage the continuation and maintenance of private-sector defined benefit pension plans".[9]

Pension derisking is where a plan sponsor lessens the risks associated with sponsoring a defined benefit plan either through in-plan solutions, such as liability driven investment, annuity buy-ins, or plan closures or freezes, or out-of-plan solutions such as lump sum offers, annuity purchases, or plan termination. "The increased PBGC premiums have 'tilted the scales' to make risk transfer look like a more cost-effective approach compared to in-plan solutions such as LDI. Eliminating benefit obligation and participant headcount allows sponsors to capitalize on short term and ongoing savings while simultaneously reducing risk."[10]

For 2024, the PBGC flat rate premium is $101 per plan participant, and the variable rate premium is $52 for every $1000 of unfunded vested benefits (i.e., under 100%) capped at $686 per participant.[11] Even for a fully funded plan that is sponsored by a financially secure employer,[12] PBGC premiums are significant. For example, for 2024, a plan with 10,000 active participants and retirees that is 120 percent funded would owe $1,010,000 in PBGC premiums,

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[8] According to its Fiscal Year (FY) 2023 Annual Report, "PBGC's Single-Employer Program remains financially healthy, with a positive net position of $44.6 billion at the end of FY 2023, up from $36.6 billion at the end of FY 2022, an improvement of $8 billion." PBGC Releases FY 2023 Annual Report Financial Positions of PBGC Insurance Programs Continue to Strengthen", Nov. 16, 2023 available at https://www.pbgc.gov/news/press/releases/pr23-048.

[9] PBGC Mission Statement available at https://www.pbgc.gov/about/who-we-are#:~:text=PBGC%20was%20created%20by%20the,insurance%20premiums%20at%20a%20minimum.

[10] "Pension De-Risking Study Analyzing the Drivers of Pension De-Rising Activity", Mercer Prepared in Partnership with the Office of the PBGC Participant and Plan Sponsor Advocate, Dec. 7, 2017 available at https://www.pbgc.gov/sites/default/files/appendix_i_-_de-risking_study.pdf.

[11] "Premium Rates: Current and Historical Information", Last Updated: Oct. 13, 2023 available at https://www.pbgc.gov/prac/prem/premium-rates.

[12] Under current PBGC premiums, whether a plan is fully funded depends on which interest rate is used. Unfortunately, because a plan must lock in which interest rate is used for five years, whether a plan is fully funded is at the whim of interest rates. This means that a plan may show up as underfunded for VRP purposes using one interest rate, but may not be using the other interest rate, but they cannot change rates for five years. See "Window of Opportunity Available for Reducing 2023 PBGC Premiums", Aug. 03, 2023 available at https://www.morganlewis.com/blogs/mlbenebits/2023/08/window-of-opportunity-available-for-reducing-2023-pbgc-premiums.

even though in this scenario there is very little chance that PBGC would ever need to pay the benefits for this plan.

Even more disturbing has been Congress' use of PBGC premiums as a budget gimmick to "pay for" other legislative initiatives unrelated to the PBGC or retirement benefits. Currently, PBGC premiums are "on budget." This means for Congressional bill scoring, an increase in PBGC premium can be used to "pay for" other unrelated government spending even though PBGC funds are not part of the general treasury and go directly from a plan sponsor to PBGC.[13] In the last decade, single-employer PBGC premiums have been raised three times, and each time was outside the context of pension reform,[14] and the increases were used as a "pay for" for other items such as transportation. If Congress is unwilling to take PBGC premiums off budget, which they were before the 1980 amendments, Congress should at least pass the Pension and Budget Integrity Act (PBIA) which would bring transparency to unvetted increases in PBGC single-employer premiums.

In 1987 the variable rate premium was introduced as an incentive for plan sponsors to better fund single employer defined benefit plans and protect the PBGC. However, as GAO noted, plan underfunding is only one risk factor, and may not in fact show the full risk to PBGC.[15] Furthermore, the variable rate premium, which was meant to protect the PBGC, whose mission it is to encourage defined benefit plan formation and maintenance, has instead encouraged plan sponsors to terminate their plans. The variable rate premium (and the funding rules) puts many plan sponsors between a rock and a hard place because they can either fund up the plan to avoid the variable rate premium or use this money for other more immediate purposes such as wages or other benefits. A plan sponsor may not need to fully fund a pension plan in one year based on the plan's demographics and the plan's cash flow needs. However, once money is in the plan, it cannot be removed other than to pay benefits or plan costs. Therefore, to avoid the VRP, a plan sponsor must fund up a plan, even though such funding may not be necessary to pay the plan costs, and, at the same time, the plan sponsor must forgo other payments, including increased wages and other benefits. Section 349 of SECURE 2.0 froze the variable rate premium at 5.2% of unfunded liabilities by no longer subjecting it to inflation, which was a step in the right direction. However, significant reform is needed to the PBGC premium structure to encourage single employer plan sponsorship.

Funding

PPA was the most significant change to the pension funding rules since ERISA was enacted in 1974. PPA was a reaction to a crisis, rather than a proactive way to improve and encourage pension plan formation. Specifically, PPA was a reaction to the stock market drop

[13] When ERISA was enacted, PGBC premiums were off budget. In 1980, Section 406 of The Multiemployer Pension Plan Amendments Act changed that so that PBGC premiums could be calculated as general fund revenue for budget scoring, even though the premiums cannot be used other than to pay benefits and PBGC administrative costs.
[14] See Moving Ahead for Progress in the 21st Century (P.L. 112-141), Bipartisan Budget Act of 2013 (P.L. 113-67), and Bipartisan Budget Act of 2015 (P.L. 114-74).
[15] "Pension Benefit Guaranty Corporation: Redesign Premium Structure Could better Align Rates with Risk from Plan Sponsors", Nov. 2012 available at https://www.gao.gov/assets/gao-13-58.pdf.

in 2001, which left all defined benefit plans underfunded at that time. Most companies were able to make up that difference, however, there were some large bankruptcies, which resulted in PBGC taking on those pension liabilities. These bankruptcies were the catalyst for PPA. Ten years after its enactment, studies showed that the defined benefit plan provisions that called for all pension plans to be funded at 100 percent regardless of the underlying demographics or the plan sponsor's financial health, actually "had the unintended consequence of worsening the nation's retirement crisis. The volatile and unworkable funding rules in the law left employers less willing to continue offering defined benefit (DB) pension plans. The law also triggered more pension 'freezes,' leaving fewer Americans with pensions."[16] According to one scholar, "the inflexibility, impenetrability, and administrative costs associated with ERISA's defined benefit minimum funding rules are, for many employers, a significant deterrent to establishing or continuing defined benefit plans, particularly when those rules are contrasted with the greater flexibility, transparency, and simplicity of the rules governing . . . 401(k) plans."[17]

This is not to say that there should not be any funding rules. However, a one size fits all approach does not work either for employers or employees, as seen from PPA. Instead, when Congress looks at the funding rules, it should recognize that "there is no single threshold that assures a healthy plan. When assessing the fiscal soundness of a pension plan, many factors should be taken into account because each situation is unique."[18] As such, any subsequent legislation should consider the pension system more holistically rather than just at an aim of protecting the PBGC through onerous funding rules on all employers.

<u>Transfers between Plans</u>

As noted above, legislation has had the unintended consequences of encouraging employers out of the defined benefit system. In many cases, plan sponsors have frozen defined benefit plans to new entrants (soft freeze) or frozen the plan both to new entrants and to future benefit accruals (hard freeze). Because of a confluence of events (such as higher investment returns and lower liabilities), some of these plans have become overfunded. However, because of the exclusive benefit rule, any excess assets may only be used for participants in that plan. But, because these plans are frozen, the participants in these plans represent a fraction of the employer's current workforce (and many do not even work for the employer because they are either retirees or individuals who have quit but have a deferred vested benefit). Current law prohibits employers from using this money to fund benefits for other employees while the plan is ongoing, and it also limits the use of it for other purposes for those in the plan to retiree health or life insurance. An employer could use the surplus to

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[16]"New Brief Examines Pension Protection Act Impacts 10 Years After Enactment", June 18, 2017 available at https://www.nirsonline.org/2017/06/new-brief-examines-pension-protection-act-impacts-10-years-after-enactment/.
[17] "The Defined Contribution Paradigm", Edward A. Zelinsky, Nov. 30, 2004 available at https://www.yalelawjournal.org/pdf/388_rys1mj7u.pdf.
[18] "The 80% Pension Funding Myth", American Academy of Actuaries, Apr. 2012 available at https://www.actuary.org/node/13461.

fund benefits for other employees to an extent, but only if the plan is terminated, which seems a draconian way to fund benefits. As such, Congress should explore ways that encourage plan sponsors to maintain frozen plans, but also allow certain amounts of excess funds to be used to pay for current employees benefits in other retirement plans sponsored by that employer.

Revisit the Prohibited Transaction Rules

ERISA and the Code categorically prohibit a litany of transactions regardless of whether a transaction is beneficial to the plan and its participants or necessary to actually run the plan.[19] For example, the prohibited transaction rules prohibit the furnishing of services between a plan and a party in interest, which includes service providers. Read literally, a plan is forbidden to employ an entity to run or administer the plan, even though there is no plan that could function without outside service providers. However, Section 408 of ERISA provides that the prohibitions in Section 406 (not just the prohibitions in 406(a)) will not apply in certain circumstances. With respect to services, the prohibition in Section 406 will not apply for "[c]ontracting or making reasonable arrangements with a party in interest for office space, or legal, accounting, or other services necessary for the establishment or operation of the plan, if no more than reasonable compensation is paid."[20] As noted below, and as illustrated by this example, there is no need for this prohibition or the exemption because entering into a contract for services that are not necessary to run the plan and/or paying more than reasonable compensation would per se be a breach of fiduciary duty of prudence under ERISA Section 404(a).

In 1995, two prominent ERISA practitioners observed that the prohibited transaction rules "increase the marginal cost of nearly every investment transaction that does not take place in public [markets]."[21] The authors reported asking "[s]everal experienced ERISA attorneys [if] they were aware of any case in which these rules had prevented or punished some abusive act that was not also proscribed by the general fiduciary rules. None could identify a single case."[22] This probably is likely because the prohibited transaction rules were not put into ERISA to protect plans or participants, but instead were a way for the tax committees to obtain jurisdiction over the legislative process as ERISA was working its way through Congress. As Frank Cummings, past Chief of Staff to Senator Jacob Javits, stated:

> Long before those fights took place, the notion of a prohibited transaction in the first place was part of the strategy of putting the whole bill—not part of the bill, the whole bill—in the Internal Revenue Code. The idea was if you were going to have fiduciary behavior standards, how in the devil could you put that in the Internal Revenue Code?

[19] See ERISA Section 406; Code Section 4975(c).
[20] ERISA Section 408(b)(2)(A).
[21] "The Regulation of Pensions: Twenty Questions after Twenty Years", 21 J. Pension Plan & Compliance, 1, 13, Kathleen P. Utgoff & Theodore R Groom (1995).
[22] "Pension Simplification", 35 J. Marshall L. Rev. 565,602-603 (2002), David A. Pratt citing Kathleen P. Utgoff & Theodore R. Groom, "The Regulation of Pensions: Twenty Questions After Twenty Years", 21 J. Pension Planning & Compliance 1, 13 (1995).

> As I recall someone had remembered that the private foundation rules, which preceded ERISA by fifteen years—was it five years? Well, it was a while.
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> But at any rate, that was the model for these prohibited transaction provisions but the provisions were really invented for the purpose of preempting the Labor Committee—so it was really part and parcel of whether the Labor or Tax Committee was going to get control of the legislation, and of course control in the tax-writing committees meant you weren't going to get a bill. So later, after they had developed a lot of this for the Internal Revenue Code, then you had to go back and fit that into Title I, but not all of the tax-prohibited transactions got back into Title I.[23]

It has been 50 years since this jurisdictional fight took place, and it is long past time for Congress to revisit the prohibited transaction rules to determine whether they actually benefit plans and participants and encourage plan formation or rather if they merely create unnecessary barriers and costs to plans because of the web of administrative and regulatory complexity that they have created.[24] Congress also should examine whether the "prohibited transaction rules are appropriate for retirement arrangements that do not involve an employer, i.e., most regular, rollover and Roth IRAs"[25]

<u>Conclusion</u>

We appreciate the Committee's attention to this important matter, and we look forward to working with you to find retirement solutions that will work for everyone.

Sincerely,

Chantel Sheaks

Chantel Sheaks
Vice President, Retirement Policy
U.S. Chamber of Commerce

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[23] "Panel 4: ERISA and the Fiduciary" available at https://drexel.edu/~/media/Files/law/law%20review/Spring2014/Panel%204_revised.ashx?la=en.
[24] There are 39 class prohibited transaction exemptions, and since 1996, DOL has issued over 1200 individual exemptions, although the number of individual exemptions has recently tapered off dramatically, even though many revised class exemptions now contain provisions making it more difficult to use the class exemption. Congress should investigate whether DOL has exceeded its statutory authority in its PTE process.
[25] "Pension Simplification" at 603.