Statement of

THE HONORABLE GORDON HARTOGENSIS

DIRECTOR

PENSION BENEFIT GUARANTY CORPORATION

before the

SENATE COMMITTEE ON FINANCE

December 11, 2019

Chairman Grassley, Ranking Member Wyden, and Members of the Committee:

Thank you for the opportunity to appear before you today. The crisis facing the Pension Benefit Guaranty Corporation's (PBGC or the Corporation) Multiemployer Program threatens the retirement security of millions of American workers, retirees, and their families.

I appreciate the work you have done to highlight this issue and hope to work with this Committee and other policymakers to find an acceptable solution. Without reforms, our Multiemployer Program — the backstop that is the last resort for retirees when a plan fails — is very likely to become insolvent by the end of 2025, which would leave participants and beneficiaries with significantly less than the level of benefits currently guaranteed by PBGC. The alarm bells are ringing, and legislative changes are necessary to protect retirees, prevent collapse of the multiemployer pension system, keep the Multiemployer Program solvent for the long term, and prevent recurrence of this crisis. As more time passes, the crisis will grow larger, more plans will deplete their assets, more retirees will lose benefits, and the cost of any fix will grow.

PROTECTING PENSIONS

PBGC recently marked its 45th anniversary. Since 1974, PBGC has played a vital role in protecting the retirement security of millions of American workers and retirees. First, as a guarantor, the Corporation provides insurance coverage for the retirement benefits of over 35 million workers and retirees who participate in private-sector defined benefit pension plans. Second, the Corporation provides retirement security for about 1.5 million participants and beneficiaries in more than 4,900 plans that have failed since PBGC was established.

Congress established PBGC as part of the *Employee Retirement Income Security Act of 1974* (ERISA). By law, the Corporation is financed from premiums and, in the case of the Single-Employer Program, assets from failed plans. PBGC is administered by a Director and has a three-member Board of Directors — consisting of the Secretary of Labor, who is the Board Chair, and the Secretaries of the Treasury and Commerce.

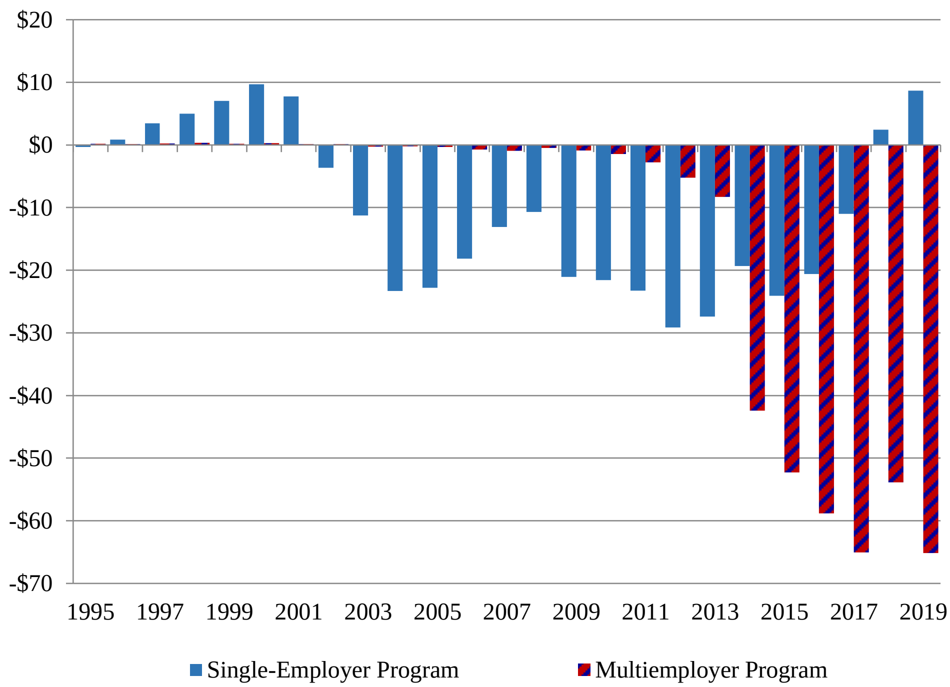
PBGC operates two separate insurance programs: one for single-employer plans (the Single-Employer Program) and one for multiemployer plans that are collectively bargained with more than one employer (the Multiemployer Program). While each program is designed to protect participants' pension benefits when plans fail, the programs 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 the insured plans.

The two programs are legally separate and operationally and financially independent. By law, assets of one program may not be used to pay obligations of the other.

Program liabilities exceeded program assets for fifteen years or longer in both of our two insurance programs until FY 2018 (see Figure 1). While the financial condition of the Single-Employer Program has been improving, the Multiemployer Program's financial condition has worsened, and the program is on a path to insolvency by the end of FY 2025.

Figure 1

PBGC Single-Employer and Multiemployer Insurance Programs
Net Positions FY 1995-2019
($ in billions)



Source: PBGC Data Tables/Annual Report

The Single-Employer Program emerged from a net negative position in FY 2018 and just completed its fourth consecutive year of improving financial results. Due in large part to Congressional action to increase employer premiums in the program, as of the end of FY 2019, the Single-Employer Program had liabilities of $119.4 billion and assets of $128.1 billion, resulting in an $8.7 billion positive net position, an improvement over a $2.4 billion positive net position at the end of FY 2018. While the financial condition of the Single-Employer Program is improving, there are still risks, like the significant amounts of underfunding in single-employer plans.

In sharp contrast to the positive net position of the Single-Employer Program, the Multiemployer Program ended FY 2019 with liabilities of $68 billion and assets of only $2.9 billion, resulting in a deficit of about $65.2 billion. The Multiemployer Program is projected to fail in just a few years.

The multiemployer pension crisis is the result of serious structural flaws in the financing of both multiemployer plans and PBGC's Multiemployer Program, which insures these plans.

Multiemployer plan funding rules permit the use of overly optimistic actuarial assumptions to determine plan liabilities and allow too much time to pay down the underfunding. Tightening these funding rules would lead to higher asset accumulations, which in turn will help plans to weather adverse financial, economic, and demographic challenges.

PBGC's Multiemployer Program is undercapitalized, with premium rates set by law that are far too low for it to provide even the modest guarantees under current law, which are significantly lower than the guarantees for single-employer plans.[1]

These structural flaws threaten pensions in multiemployer plans that are seriously underfunded today, and they set the stage for similar crises in the future.

I will first discuss multiemployer plans and the structural flaws that have put over a million workers and retirees at risk of pension losses due to future insolvency of their plans.

MULTIEMPLOYER PLANS

A multiemployer plan is a pension plan to which more than one employer is required to contribute and which is maintained through one or more collective bargaining agreements between the contributing employers and one or more employee organizations or unions. The employers are usually in the same or related industries. These plans provide benefits for people in industries such as transportation, construction, mining, and hospitality. They are jointly administered and governed by an independent board of trustees, with an equal number of labor and management representatives.

[1] For example, the maximum guaranteed benefit for a multiemployer plan retiree with 30 years of service is $12,870 annually. In contrast, the maximum guaranteed benefit for a retiree at age 65 in a single-employer plan that fails in 2020 is $69,750 annually. The guarantee is lower for those who retire early or when there is a benefit for a survivor.

Multiemployer plans have provided retirement benefits to millions of American workers for more than half a century. Today, there are roughly 1,400 multiemployer plans that provide retirement security to about 10.8 million participants and their families.

These plans cover participants in every state and range in size from small local plans with a hundred or fewer participants to large national plans covering hundreds of thousands of participants. Businesses of all sizes, including hundreds of thousands of small businesses, participate in multiemployer plans.

From the perspective of workers, multiemployer plans provide pension portability, allowing them to accumulate benefits earned for service with different employers throughout their careers. From the perspective of employers — especially small employers — a multiemployer plan could provide efficiencies of scale compared to a single-employer plan: less administrative burden and cost, more diversified and less costly investment opportunities, and pooled longevity risk, which helps reduce costs. Unfortunately, these theoretical advantages have been more than offset by structural flaws in how the plans have been operated and financed.

Funding rules for multiemployer plans — which differ considerably from the rules for single-employer plans —have resulted in valuations of liabilities that significantly understate the actual cost of plan benefits. Pension funding requirements should lead to benefit security, because retirees understandably expect their pensions will be paid as promised and not be subject to risk. But those expectations are not reflected in today's permissive multiemployer funding rules. That is especially dangerous in the multiemployer context, where the guarantee is significantly lower than the guarantee for other defined benefit plans. In addition, multiemployer plans are afforded too much time to pay down underfunding. The rules allow underfunding that results from benefit improvements or adverse experience (such as investment returns or employer contributions that were lower than anticipated) to be paid for over a 15-year period (rather than the 7-year period used for single-employer plans).

This extended period of time makes it difficult or even impossible for some plans to make up for the actuarial losses, including the loss of contributions that results from competition, declines in demand for products or services, and technological changes. These same factors also caused some companies to go out of business, leaving behind the unfunded benefits of their inactive and retired workers (sometimes referred to as orphan liabilities) for other contributing employers to inherit.

A significant percentage of multiemployer plans have been unable to attain financial stability after the 2009 financial crisis, despite a strong economy bolstered by the *Tax Cuts and Jobs Act*. As plans struggle to improve funded status, contributing employers that remain in these plans are often faced with the difficult choice between continuing to participate in the plan (with the prospect of being required to increase their contributions) or withdrawing from the plan and incurring withdrawal liability.

About 125 plans, some very large, covering 1.4 million participants, are now in Critical and Declining status,[2] which means that plan insolvency is projected to occur within 20 years or less.[3] The underfunding in all Critical and Declining plans totals about $100 billion when measured on a market basis.[4]

These plans will not be able to provide promised benefits without help from the Multiemployer Program. But the Multiemployer Program, as currently financed, cannot be the safety net it purports to be and on which millions of workers, retirees, and families depend.

MULTIEMPLOYER PROGRAM

PBGC's Multiemployer Program provides financial assistance[5] to insolvent multiemployer plans so that they can pay benefits at PBGC guaranteed levels.[6] The Multiemployer Program is funded by premiums paid by the plans, but this program will also run out of money in a few years, jeopardizing retirement security of workers in failing plans as well as plans currently receiving financial assistance from PBGC.

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.

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.

At the end of FY 2019, PBGC was liable for $2.8 billion for plans already receiving financial assistance, as well as $65.2 billion booked as "probable" obligations for plans that are expected to become insolvent in the next ten years or are terminated but not yet insolvent. The ten largest plans classified as probable obligations account for $53.6 billion of the $65.2 billion total probable obligations. In addition to the $68.0 billion booked as a liability in our financial statements, there is $10.9 billion in liabilities for future financial assistance to ongoing multiemployer plans projected to become insolvent in the next 10 to 20 years; these plans, which are not booked as liabilities, are classified as "reasonably possible" future obligations.

As plans become insolvent, the Multiemployer Program's assets will be exhausted, and only premium income will be available to pay financial assistance.

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[2] Based on Form 5500 information and the Critical and Declining Notices filed as of December 2018.

[3] Under ERISA § 305(b)(6), which was added by the Multiemployer Pension Reform Act of 2014 (MPRA), a plan is in critical and declining funded status for a plan year if the plan's actuary determines that the plan meets certain conditions indicating significant underfunding, and it is projected to become insolvent during the current plan year or any of the 14 succeeding plan years (19 succeeding plan years if the plan has a ratio of inactive participants to active participants that is greater than two to one or if the funded percentage of the plan is less than 80%).

[4] According to PBGC analysis of 2017 Form 5500 data, critical and declining plans have $106.7 billion in unfunded current liability.

[5] Financial assistance also covers reasonable administrative expenses.

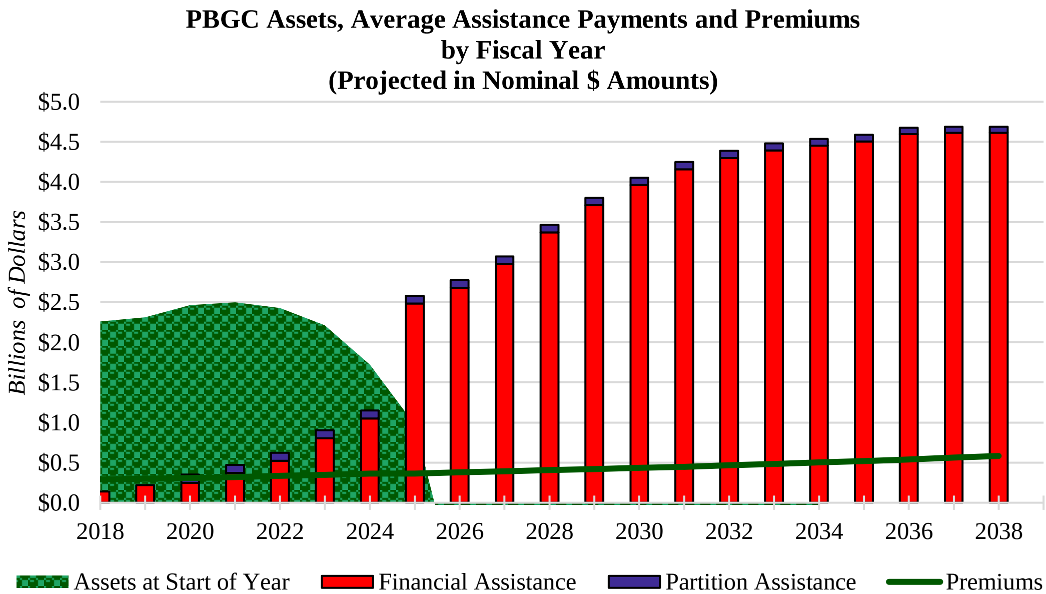
[6] PBGC financial assistance is technically a loan to the insolvent plan. But because the plans have already run out of money, repayment of financial assistance loans is highly unlikely. To date, only one loan has been repaid, and that loan was made in the circumstance of a plan having a temporary financial need rather than a permanent one.

That means plan participants will see a substantial reduction in the benefits they receive — mere pennies on the dollar. The backstop that hardworking men and women had been depending on for a secure retirement — and to help support themselves and their families — simply won't be there.

Let me be as clear as I can. Unless Congress acts, participants in insolvent plans will receive next to nothing. A typical retiree with 30 years of accrued benefits would receive only about $100 a month.

The Multiemployer Program is estimated to have a 99 percent likelihood of insolvency by the end of FY 2025 and a100 percent likelihood in FY 2026. The likelihood of insolvency does not vary greatly with the expected future use of suspension and partitions under the *Multiemployer Pension Reform Act of 2014* (MPRA) (see Figure 2 below). The projections assume a zero percent likelihood that the largest critical and declining plan will suspend benefits, a 30 percent likelihood that other plans will apply for suspension alone, and a 10 percent likelihood that other plans will apply for both suspension and partition. These percentages reflect our best estimates based on experience to date under MPRA.[7] No scenario in our modeling shows the Multiemployer Program remaining solvent beyond FY 2026 under current law.

Figure 2

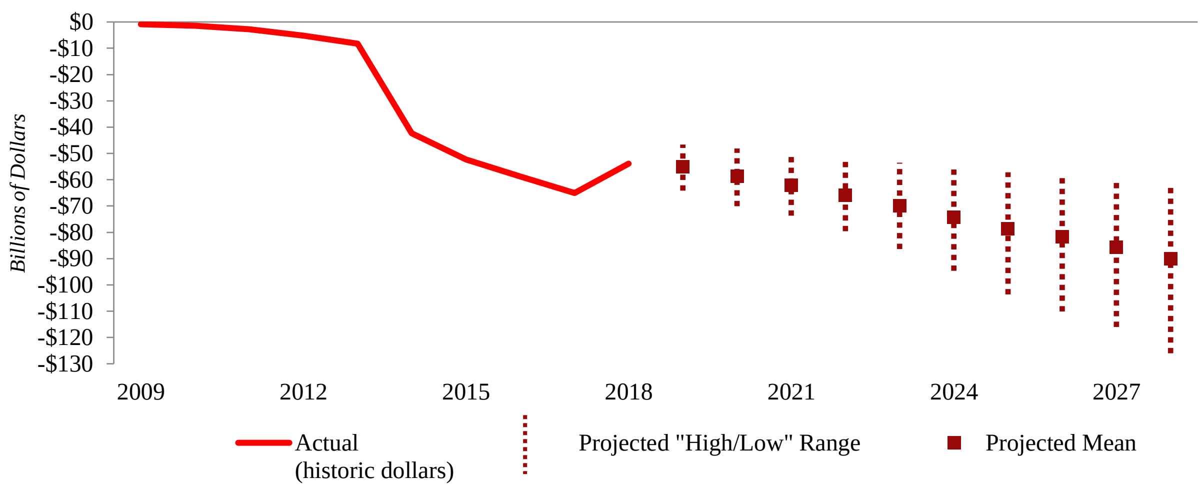


[7] The "best estimate" of MPRA utilization in the FY 2014 Projections Report was a 100 percent likelihood that the Central States Pension Fund, the largest critical and declining plan will suspend benefits, a 60 percent likelihood that other plans will apply for suspension alone, and a 20 percent likelihood that other plans will apply for both suspension and partition. The report also contained an "alternative" that halved these assumptions. The FY 2015 Projections Report (issued June 6, 2016) used revised assumptions to reflect that (1) the Central States Pension Fund's application for benefit suspension was rejected (May 6, 2016) and the plan announced that it would not reapply and (2) the rate of applications from other plans had been less than initially expected. Those revised assumptions are reviewed every year and remained in effect for the FY 2018 Projections Report.

PBGC's FY 2018 Projections Report shows a projected FY 2028 year-end mean deficit of about $90 billion (in nominal dollars) in the Multiemployer Program, even if some additional plans use benefit suspensions and partitions as allowed under the MPRA to avoid insolvency (see Figure 3 below).

Figure 3

Multiemployer Program Net Position
Historical Experience 2009-2018 and Nominal 2019-2028 Projections



The dire state of the Multiemployer Program reflects both the structural flaws in the funding rules for multiemployer plans and PBGC premiums that have been too low for decades and do not take into account the risk posed by individual plans. As a result, multiemployer premiums fall short of the financial needs of the program and offer no incentive to improve plan funding (see Figure 2).

In contrast to the Single-Employer Program, which assesses a variable-rate premium based on plan underfunding in addition to a flat-rate per-participant premium, multiemployer plans pay only a flat-rate per participant premium.

For plan years beginning in 2020, per year single-employer plan sponsors will pay a flat-rate premium of $83 per participant and a variable-rate premium of $45 per $1,000 of plan underfunding, capped at $561 per participant; all rates for future years are indexed. By contrast, the flat-rate multiemployer premium for plan years beginning in 2020 is $30 per participant per year and is indexed for future years. As the green line in Figure 2 shows, premium income under current law will pay only a small fraction of the financial assistance needed for insolvent plans to pay benefits at PBGC-guaranteed levels.

CONSEQUENCES OF MULTIEMPLOYER PROGRAM INSOLVENCY

Insolvency of PBGC's Multiemployer Program will dramatically reduce the already relatively low guarantee for multiemployer plan participants. Under current law, when Multiemployer Program assets are exhausted, the only money available to provide financial assistance for benefit payments will be incoming multiemployer premiums.

The Multiemployer Program will soon be spending more in financial assistance than it receives in premium income. The Multiemployer Program's resources will represent only a small fraction of the amount required to pay benefits at current guarantee levels. Under the program's authorizing legislation,[8] PBGC would submit to Congress, in advance of Multiemployer Program insolvency, schedules of premium increases needed to provide current guarantees and reduced guarantees that would be necessary in the absence of a premium increase. Such reduced guarantees would result in participants in failed multiemployer plans receiving a very small fraction of the current guarantee level, no matter when their plan became insolvent.

FINDING A PATH FORWARD

PBGC works with troubled multiemployer plans and their sponsors who come to us seeking to prevent plan insolvency. But the tools the Corporation has to address the multiemployer crisis are limited, and legislation is needed to prevent the looming insolvency of PBGC's Multiemployer Program. Both Congress and the Administration have recognized this fact.

Joint Select Committee

In 2018, Congress created the Joint Select Committee on Solvency of Multiemployer Pension Plans to develop recommendations to address the problems in the multiemployer pension system. While the Committee did not issue recommendations before its term expired on November 30, 2018, it succeeded in creating a broader understanding of the issues and potential reforms. I would like to thank the members of that Committee for the work they did as part of that effort.

President's FY 2020 Budget Proposal

The President's FY 2020 Budget includes a proposal to shore up PBGC's Multiemployer Program. The Budget proposes adding a variable-rate premium on unfunded benefits, similar to the Single-Employer Program, with provision for waivers to avoid accelerating insolvency in the most troubled plans. The proposal also includes an exit premium on companies that withdraw from multiemployer plans. It is estimated to raise an additional $18 billion over the ten-year budget window.

The Administration's Framework for Reform

The Administration stands ready to work with Congress on a long-term solution that appropriately balances the interests of all those affected by the multiemployer pension system — from retirees, workers, employers, and unions to plans and taxpayers. That solution should raise the federal pension guarantee limit to improve retirement security, fix the defects in the system to prevent the crisis from recurring, give PBGC the tools to mitigate risks, and limit the burden on taxpayers. The proposal from Chairmen Grassley and Lamar Alexander appears to share these goals, and the Administration looks forward to learning more about this proposal.

The Administration believes a solution should simultaneously accomplish several goals: protect retirees and prevent the collapse of the multiemployer pension system, save the federal backstop, and prevent a future crisis.

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[8] ERISA § 4022A(f)(2).

- Protect Retirees and Prevent Collapse: Expanding PBGC's current ability to partition multiemployer pension plans would provide needed financial assistance to distressed plans. PBGC financial assistance could subsidize a plan's benefit payments so the plan could remain solvent. This relief would be accompanied by conditions and reforms to limit the burden on taxpayers and to ensure that plans are governed responsibly to protect retirees' benefits.

- Save the Federal Backstop: Any responsible solution requires new sources of revenue for PBGC, and the greater share of the cost should be borne by those who promised underfunded pension benefits and those protected by the Corporation's guarantee. A solution will require compromise by all parties concerned with the troubled multiemployer pension plan system and more accurately charge insurance premiums based on risk.

- Prevent Future Crisis: A responsible proposal must come with strong protections to prevent a repeat of this crisis — including policies to hold plans accountable, provide proactive authorities to PBGC, improve transparency and disclosure, and remove legal and regulatory barriers to promote innovation in the retirement system. Additionally, reforms should establish guardrails to ensure plan benefits are funded as they are earned, including regulating plan assumptions regarding investment returns and levels of industry economic activity.

Together, these commonsense reforms will help provide a lasting solution that protects retirees, prevents the collapse of pension plans, secures the future of PBGC, and avoids future crises in the multiemployer system. This is the lens through which the Administration will evaluate proposed solutions.

Current Legislative Proposals

While a number of legislative proposals have emerged to address the multiemployer pension crisis, those that have been seriously considered by Congress have either been insufficient or not comprehensive.

In July, the House of Representatives passed H.R. 397, the *Rehabilitation for Multiemployer Pensions Act*. This legislation would provide taxpayer-funded loans and PBGC financial assistance in an attempt to prevent the insolvency of troubled plans. It would also establish a new agency at Treasury to administer this loan program and provide general revenues to PBGC to fund financial assistance.

H.R. 397 may be well-intended, but it is not the solution taxpayers, workers, and retirees need. The Congressional Budget Office (CBO) estimated that the bill's loan and financial assistance provisions would cost approximately $68 billion, including the long-term cost of the loan program and the first 10 years of new PBGC financial assistance. Furthermore, the bill is unlikely to solve the fundamental problem. In a September letter to Senator Mike Enzi, CBO predicted that a quarter of the plans would be unable to repay their loans and most of the remaining plans would go broke within 10 years after the loan period.

Unfortunately, this legislation contains no reforms that would protect workers, retirees, and taxpayers from more plan failures and more bailouts.

Another proposal is S. 2788, the *Bipartisan American Miners Act*. This legislation, introduced just last month, would help protect the retirement security of more than 90,000 miners and their families who participate in the failing United Mine Workers of America 1974 Pension Plan, which has nearly no remaining contributing employers outside of bankruptcy. However, passage of this legislation would not materially alter the timing of PBGC's expected insolvency or provide assistance to other multiemployer plans.

The Start of a Solution

The "Multiemployer Pension Recapitalization and Reform Plan" takes a commonsense, pragmatic, and forward-thinking approach to comprehensive reform. As Chairmen Grassley and Alexander outlined when they released the plan in November, the proposal is built on five major components: stabilize plans in immediate danger of failure; secure workers' and retirees' benefits; strengthen PBGC's ability to backstop the multiemployer system; put the system on a stable long-term path; and ensure fiscal responsibility. These components are closely aligned with the Administration's principles for reform, and a closer look at the Grassley-Alexander plan's proposal reveals a number of specific reforms worth noting.

For one, it would provide a stronger guarantee for participants and create a better financial base for the future. It would expand PBGC's current partition authority, which will allow the Corporation to better help plans in declining status. Additionally, the proposal would substantially increase PBGC's maximum benefit guarantee for multiemployer plans, which is currently lower than the guarantee for the significantly healthier Single-Employer Program. That means that, if a plan becomes insolvent, retirees can receive significantly more in guaranteed pension benefits than the law currently allows — and orders of magnitude more than if the Multiemployer Program itself runs out of money.

The Grassley-Alexander proposal also addresses a critical question: how to pay for these reforms. The proposal would establish a new premium structure that would make it possible for the Corporation to financially assist troubled plans, generating the revenue needed to improve our overall financial position. It also introduces a new stakeholder co-payment, which means there will be a shared responsibility for these costs. While cash flows for any given year are difficult to project, on an aggregate basis, PBGC estimates the proposal should provide enough income to pay the costs of partition and the higher guarantee into the late 2030s.

Finally, the proposal includes a number of measures that will help create a sustainable multiemployer pension system for years to come, such as providing workers and employers a new, attractive retirement plan option. It also includes reforms to improve funding and liability measurement rules, strengthen the zone-status rules to make them more effective, and enhance and clarify the withdrawal liability rules. Importantly, the proposal also includes reforms to improve plan management, ensure greater accountability, and give PBGC more authority to supervise multiemployer plans. These reforms will help protect taxpayers from the consequences of continuing plan failures.

The Administration views the “Multiemployer Pension Recapitalization and Reform Plan” as a welcome starting point for a serious conversation about reforms to the multiemployer pension system. We believe it has the potential to serve as the base for a long-term solution to the multiemployer pension crisis. It also includes concepts and proposals that may require further analysis and adjustment to ensure it ultimately becomes effective, bipartisan legislation.

CONCLUSION

The PBGC’s Multiemployer Program and many multiemployer plans are headed toward collapse. Our projections show insolvency of PBGC’s Multiemployer Program by the end of the fiscal year ending September 30, 2025.

If the PBGC’s 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 guarantee will then be funded. The result will be catastrophic for many people — current and former workers, small business owners, retirees, beneficiaries, and their families.

It’s clear that legislative action is necessary; it’s important that policymakers come to an agreement on the right solution, and that they do so soon.

I appreciate the leadership of Chairman Grassley, Ranking Member Wyden, and the Members of this Committee in addressing the challenges faced by multiemployer plans and the PBGC Multiemployer Program.

Chairman Grassley and Chairman Alexander’s proposal contains the beginnings of a solution that is balanced, will keep the Multiemployer Program solvent, deliver meaningful benefit protection to workers and retirees, and put multiemployer plans on a course toward funding improvements over the long term. I am eager to work with you, other Members of Congress, and stakeholders to safeguard pension benefits and 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.