



U.S. SENATE COMMITTEE ON

Finance

SENATOR CHUCK GRASSLEY, OF IOWA - CHAIRMAN

<http://finance.senate.gov>

MEMORANDUM

To: Reporters and Editors
Re: Pension legislation substance
Da: Thursday, June 9, 2005

Sen. Chuck Grassley, chairman of the Committee on Finance, today made the following comment on the substance of the pension legislation he is drafting. Grassley is refining the pension bill he introduced in January in light of recent developments.

“As the Finance Committee’s investigation of United Airlines’ pension default and the GAO’s recent report on the pension crisis have made painfully clear, we need completely new rules requiring accurate measurement of pension liabilities and full funding of all pension plans. The legislation I’m drafting will do just that. It’ll adopt the Administration’s yield curve proposal and eliminate the so-called ‘smoothing’ techniques that let companies hide massive pension losses from their employees and the public at large.”

Following is information on his bill introduced in January.

For Immediate Release

Monday, Jan. 31, 2005

Grassley, Baucus Re-introduce NESTEG Pension Bill,
Announce Plans to Look at More Reforms

WASHINGTON – Sen. Chuck Grassley, chairman of the Committee on Finance, and Sen. Max Baucus, ranking member, today re-introduced their pension protection legislation -- the *National Employee Savings and Trust Equity Guarantee (NESTEG) Act* – which received unanimous Finance Committee support last year but never won final approval.

The NESTEG bill would expand protections for retirement plan participants and require companies to allow their employees to diversify out of company stock, adopt a permanent yield curve replacement for the 30-year Treasury rate used for pension funding purposes, expand the portability of retirement plan assets, and simplify pension laws and regulation.

“I’ve worked in the Finance Committee on several pieces of legislation signed into law in

response to the scandals at Enron and other corporations,” Grassley said. “The important pension protections in the NESTEG bill are one remaining area for reform. This is ‘must-pass’ legislation this year. The headlines have died down, but workers’ pensions are still too vulnerable to executive greed. It’s also critically important to remove the uncertainty in our pension system by enacting a permanent replacement to the 30-year Treasury rate for pension funding. Workers need reliable pension funding, and employers need a reliable basis on which to calculate pension payments.”

Baucus said, “I join Senator Grassley in urging rapid passage of this legislation. We must act before another corporate scandal devastates more workers’ retirement security. We must make pensions more secure for workers while simplifying administration for employers. The bill we are introducing today is a big step in that direction.”

Last year, Congress approved a temporary replacement of the 30-year Treasury rate with a long-term corporate bond rate for pension funding purposes. The NESTEG bill includes a permanent replacement of the 30-year Treasury rate with a yield curve based on corporate bond rates.

In addition, Grassley and Baucus said they expect the committee to consider additional pension funding reforms in light of concerns regarding pension under-funding and the financial health of the nation’s pension insurer, the Pension Benefit Guaranty Corporation (PBGC). The PBGC’s deficit has increased from \$11 billion to \$23 billion in the course of a year, and was in surplus as recently as 2001.

“We need to be sure our nation’s pension plans are fully funded,” Grassley said. “When companies fall short in their pension payments, workers end up on the short end of the stick in retirement. We also need to do all we can to get the PBGC back on a strong financial footing.”

Baucus said, “We must strengthen the funding of defined benefit plans so workers can count on their pension benefits. Retirement is not the time to find out you have planned your financial life around a hollow promise.”

Grassley and Baucus also expect the committee to look at new, innovative ways to increase savings.

“We all know Americans should be saving more,” Grassley said. “There are a lot of creative ideas out there for boosting savings, and I look forward to working with members of the Finance Committee on ways to do that.”

Baucus said, “We all agree on the need for a real increase in retirement savings. I am committed to developing ways to create new savings, and help Americans look forward to a more secure retirement.”

A section-by-section summary of NESTEG follows.

Summary

National Employee Savings and Trust Equity Guarantee Act of 2005 (NESTEG)

TITLE I -- PROVISIONS RELATING TO INVESTMENT OF PARTICIPANTS' ACCOUNTS

Subtitle A -- Diversification Of Pension Plan Assets

Sec. 101. Defined contribution plans required to provide employees with freedom to invest their plan assets.

The bill generally provides that publicly held companies must allow workers to divest themselves of company stock attributable to employer contributions once they have completed 3 years of service. Accounts attributable to employee contributions could be diversified immediately. There is a 3-year phase-in for stock contributed to employer accounts in previous years, except participants who are 55 years old with 3 years of service can diversify immediately. Only free-standing Employee Stock Ownership Plans and single-participant plans are exempt from the requirement.

Sec. 102. Notice of freedom to divest employer securities or real property.

Participants must be notified of the right to divest at least 30 days before the date the participant is first eligible to do so. The notice will describe the importance of diversification. A model notice will be prescribed by the Secretary of Labor. Penalties apply to failure to give notice.

Subtitle B -- Information To Assist Pension Plan

Participants

Sec. 111. Periodic pension benefit statements.

The bill requires quarterly benefit statements for defined contribution plans that allow workers to direct their own investments, annual statements for plans that do not allow worker investment direction, and once every 3 years to workers in defined benefit plans. In addition to the market value of investments, individually directed plan participant statements would include a description of any restrictions on the right to direct investments, and a notice that investments may not be adequately diversified if over 20% of the account is in one investment.

Sec. 112. Defined contribution plans required to provide adequate investment education to participants.

All workers must receive annual investment guidelines and retirement planning information. The Secretary of Labor will develop a model form, worksheet and internet calculators.

Sec. 113. Material information relating to investment in employer securities.

The bill requires sponsors of defined contribution plans to make sure that all material information the employer is required to disclose to investors under the securities laws also be provided to workers concerning investments in company stock in the worker's account.

Sec. 114. Fiduciary rules for plan sponsors designating independent investment advisors.

If certain rules are followed, plan sponsors would not be liable for investment advice provided by a qualified investment adviser to participants in a self-directed individual account plan.

Sec. 115. Treatment of qualified retirement planning services.

Employers would be permitted to offer qualified retirement planning services to employees on a salary reduction basis, with a limit of \$1,000 per year.

Subtitle C -- Protection Of Pension Plan Participants

Sec. 121. Notice to participants or beneficiaries of blackout periods.

An excise tax is added to the Code for failure to provide a blackout notice. Minor corrections to the ERISA provision added in Sarbanes Oxley are also included.

Sec. 122. Allowance of catch-up payments.

An eligible individual would be permitted to make additional contributions to an IRA up to \$1,500 per year in tax year 2005 and \$3,000 in tax years 2006 through 2009. Eligible individuals were participants in a 401(k) or similar plan, with a matching contribution from a currently bankrupt employer, and the employer is currently under indictment or subject to conviction.

TITLE II -- PROVISIONS RELATING TO FUNDING, DEDUCTIONS, AND THE PENSION BENEFIT GUARANTY CORPORATION

Subtitle A – Replacement of Interest Rate on 30-Year Treasury Securities

Sec. 201. Replacement of interest rates on 30-year Treasury securities used for purposes of funding and PBGC premium rates.

The interest rate used for funding requirements and PBGC premiums is changed for plan years beginning after December 31, 2005. For years beginning before December 31, 2006, the proposal replaces the 30-year Treasury rate with the rate of interest on amounts conservatively invested in long-term corporate bonds. For funding purposes, the maximum permissible rate will be 100% of the 4 year weighted average of this rate. A similar provision, effective for only 2004 and 2005, was enacted into law in H.R. 3108.

For plan years beginning after December 31, 2006, the interest rate used for purposes of funding requirements, PBGC premiums and determining lump sum distributions is based on a yield curve reflecting interest rates on corporate bonds of various durations. Under the proposal the yield curve is phased in at a rate of 20 percent each year over five years. During the phase in period, the rate used is based on a combination of the yield curve and the previously applicable rate. For determining funding requirement and PBGC premiums, the previously applicable rate is the rate of interest on amounts conservatively invested in long-term corporate bonds. For purposes of determining lump sum distributions, the previously applicable rate is the 30-year Treasury rate. The yield curve is completely phased in for years beginning after December 31, 2010.

The Secretary of the Treasury is directed to prescribe by regulations a method for determining the rates of interest. The Treasury Department is also directed to issue recommendations for changes in funding rules to strengthen funding, and disclosure of funded status.

Sec. 202. Replacement of 30-Year Treasury rate for calculating lump distributions.

See section 201 above.

Sec. 203. Section 415 limitation on defined benefit plans.

The interest rate used to determine maximum benefit payment will be fixed at 5.5%.

Subtitle B – Provisions Relating to Pension Plan Funding and Deductions

Sec. 211. Deduction limits for plan contributions.

To allow employers to contribute more in good times, the maximum deductible contribution to a defined benefit plan would be increased to allow employer to fund up to 130% of current liability instead of the current 100%.

Sec. 212. Benefit limitations for certain financially distressed plans.

Plans of employers with junk bond ratings will have to freeze accruals if vested benefits are less than 50% funded. These plans will also be prohibited from making lump sum payments in excess of \$5,000. The freeze applies to negotiated plans on the first day of the next collective bargaining agreement. For other plans, it applies on the first day of the next plan year.

Sec. 213. Updating deduction rules for combination of plans.

Employer contributions to defined contribution plans of up to 6% of compensation would be deductible, regardless of the amount of defined benefit contributions. Matching contributions that are not deductible solely because of the combined plan limitation would not be subject to the 10% excise tax on non-deductible contributions.

Subtitle B – Provisions Relating to Pension Benefit Guaranty Corporation

Sec. 221. PBGC premium for new plans of small employers.

Reduces the basic PBGC premium for new small employer (100 or fewer employees) plans from \$19 per person to \$5 per person for the first 5 years of the plan's life.

Sec. 222. Additional PBGC premium for new and small plans.

Five-year phase in of PBGC premium for new plans and special rule for new plans of very small employers.

Sec. 223. Authorization for PBGC to pay interest on premium overpayment refunds.

Allows PBGC to pay interest on premium refunds at the rate charged for underpayments.

Sec. 224. Substantial owner benefits in terminated plans.

Guaranteed benefits for majority owners (50% or more ownership) would phase in over 10 years. Existing law provides a phase in over 30 years for "substantial owners" (more than 10% owners.)

Sec. 225. Acceleration of computation of benefits attributable to recoveries of employer liability.

In order to expedite payments, PBGC would be permitted to estimate the amount of benefits payable to participants in PBGC-trusted plans. Adjustments would be made when final calculations are available.

Subtitle D – Studies

Sec. 231. Joint study on revitalizing defined benefit plans.

Sec. 232. Study on floor-offset ESOP's.

TITLE III – IMPROVEMENTS IN PORTABILITY AND DISTRIBUTION RULES

Sec. 301. Clarifications regarding purchase of permissive credit.

This provision clarifies rules regarding purchase of service credit from a sec. 403(b) annuity or a sec. 457 plan to a governmental defined benefit plan. Purchase of service is permitted by participants in these plans. In the case where service is performed as an employee of an educational organization providing elementary or secondary education, service can be determined under the law of any State or nation.

Sec. 302. Allow rollover of after-tax amounts in annuity contracts.

Sec. 303. Clarification of minimum distribution rules.

The proposal directs the Secretary of the Treasury to issue regulations under which a governmental plan is treated as complying with minimum distribution rules, for all years to which such requirements apply, if the plan complies with good faith interpretation of the statutory requirements.

Sec. 304. Waiver of 10 percent withdrawal penalty tax on certain distributions of pension plans for public safety employees.

Reduces from 55 to 50 the age at which public safety employees can take penalty-free lump sum withdrawals of lump sum benefits from governmental defined benefit plans.

Sec. 305. Allow rollovers by non-spouse beneficiaries of certain retirement plan distributions.

Benefits payable from a qualified retirement plan, governmental 457(b) plan or tax sheltered annuity could be transferred to an inherited IRA for a non-spouse beneficiary.

Sec. 306. Faster vesting of employer nonelective contributions.

Nonelective employer contributions would be subject to the same minimum vesting rules as matching contributions (6 year graded or 3 year cliff).

Sec. 307. Allow direct rollovers from retirement plans to Roth IRAs.

Eligible rollover distributions could be deposited directly to a Roth IRA instead of having to be first deposited to a traditional IRA, then transferred to a Roth.

Sec. 308. Elimination of higher penalty on certain simple plan distributions.

The 20% early distribution penalty applicable to SIMPLE plans for an initial 2 year period would be reduced to 10%.

Sec. 309. Simple plan portability.

The bill would permit rollovers between SIMPLE plans and other tax-favored retirement

arrangements within the first two years of participation.

Sec. 310. Eligibility for participation in retirement plans.

Distributions under former Sec. 457(e)(9) (pre-SBJPA 96) would not preclude participation in an eligible non-governmental 457 plan.

Sec. 311. Transfers to the PBGC.

Automatic rollovers of involuntary distributions could be transferred to PBGC instead of to an IRA.

Sec. 312. Missing participants

PBGC has maintained a “Missing Participant Program” that holds and pays benefits to missing participants of terminated single-employer defined benefit plans covered by PBGC, but other plans have had no help available. The bill would extend this program to terminated plans of private employers not covered by PBGC, including defined contribution plans. PBGC would also be directed to set up a similar program for multiemployer plans.

TITLE IV – ADMINISTRATIVE PROVISIONS

Sec. 401. Employee Plans Compliance Resolution System.

The Employee Plans Compliance Resolution System (EPCRS) allows plan sponsors to correct operational violations with regard to qualified retirement plans without risking plan disqualification. Treasury is directed to update and improve the program with regard to small business plan sponsors.

Sec. 402. Extension to all governmental plans of moratorium on application of certain nondiscrimination rules applicable to State and local plans.

All government plans would be treated like state and local government plans for purposes of not having to comply with certain non-discrimination rules.

Sec. 403. Notice and consent period regarding distributions.

The bill extends the benefit election period from 90 days to 180 days. In addition, participants must be notified of the right to defer payment, if deferral is available and of the impact of failing to defer payment.

Sec. 404. Reporting simplification.

Raises the asset limit for the 5500-EZ to \$250,000, and requires Treasury and DOL to develop a simplified 5500 form for plans with 25 or fewer participants.

Sec. 405. Voluntary early retirement incentive and employment retention plans maintained by local educational agencies and other entities.

This provision addresses two issues that affect teachers: retirement plans for that provide retention bonuses, and plans that provide early retirement incentives. Retention bonuses would be treated as severance pay instead of deferred compensation, and early retirement incentives could be age-related.

Sec 406. No reduction in unemployment compensation as a result of pension rollovers.

States would be prohibited from treating rollovers as income in determining unemployment compensation.

Sec. 407. Withholding on distributions from governmental section 457 plans.

Grandfather's certain distributions, exempting them from withholding requirements imposed by EGTRRA.

Sec. 408. Provisions relating to plan amendments.

TITLE V – PROVISIONS RELATING TO SPOUSAL PENSION PROTECTION

Subtitle A – Study of Spousal Consent for Distributions From Defined Contribution Plans

Sec. 501. Joint study of application of spousal consent rules to defined contribution plans.

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Subtitle B -- Division of Pension Benefits Upon Divorce

Sec. 511. Regulations on time and order of issuance of domestic relations orders.

Directs DOL to issue regulations to clarify that a domestic relations order issued subsequent to a divorce can be a Qualified Domestic Relations Order (QDRO).

Subtitle C – Railroad Retirement

Sec. 521. Entitlement of divorced spouses to railroad retirement annuities independent of actual entitlement of employee.

Extension of tier II railroad retirement benefits to surviving former spouses pursuant to divorce agreements.

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Subtitle D -- Modifications of Joint and Survivor Annuity Requirements

Sec. 531. Requirement for additional survivor annuity option.

Mandates an alternative joint and survivor annuity option under pension plans that do not fully subsidize the qualified joint and survivor annuity.

TITLE VI -- TAX COURT PENSION AND COMPENSATION

Conforms retirement and benefit programs of the Tax Court to those of Article III Courts.

TITLE VII -- OTHER PROVISIONS

Sec. 701. Transfer of excess pension assets to multiemployer health plan.

Extends the ability to make Sec. 420 excess asset transfers to certain multiemployer plans.

Sec. 702. Transfer of excess funds from black lung disability trusts to United Mine Workers of

America Combined Benefit Fund.

Eliminates the aggregate limit on the amount of excess black lung benefit trust assets available to pay premiums, and transfers the additional amounts available to the UMWA Combined Benefit Fund.

Sec. 703. Treatment of death benefits from corporate-owned life insurance.

Limits the availability of tax-free proceeds on company-owned life insurance, and provides disclosure and reporting requirements.