RSC
Republican Study Committee
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Legislative Bulletin…………………………….………December 15, 2005

Contents:

Summary of the Bill Under Consideration Today:

Total Number of New Government Programs: 0

Total Cost of Discretionary Authorizations: $0

Effect on Revenue: $14.2 billion decrease over five years; $71.8 billion decrease over ten years

Total Change in Mandatory Spending: $3.0 billion decrease over five years; $305 million decrease over ten years

Total New State & Local Government Mandates: 0

Total New Private Sector Mandates: At least 8 (though some of these are adjustments to existing mandates)

Number of *Bills* Without Committee Reports: 0

Number of *Reported* Bills that Don't Cite Specific Clauses of Constitutional Authority: 0

H.R. 2830—Pension Protection Act—*as reported* (Boehner, R-OH)

Order of Business: The bill is scheduled to be considered on Thursday, December 15th, subject to a closed rule self-executing an amendment in the nature of a substitute that includes a few changes agreed to in the much-publicized deal with the United Auto Workers. The vast majority of the underlying bill will remain unchanged. More information will be provided on the rule and the changes the amendment would make to the base bill in a separate RSC document Thursday morning.

Summary by Title: H.R. 2830 would amend the Employee Retirement Security Act of 1974 (ERISA) and the Internal Revenue Code of 1986 to reform the funding rules for pensions. Highlights of the bill, as jointly reported by the Education and the Workforce Committee and the Ways and Means Committee, are as follows:

Title I: Reform of Funding Rules for Single-Employer Defined Benefit Pension Plans

- Repeals ERISA's minimum funding standards that single-employer defined benefit plans must meet and creates new standards.

- Requires that an employer make the minimum contributions to a plan, subject to certain Treasury Department waiver authority in cases of business hardship (when the employer is operating at an economic loss, when there is substantial unemployment or underemployment in the relevant industry, when the sales and profits of the industry are depressed or declining, and when it is reasonable to conclude the plan will be continued only if the waiver is granted).

- Requires that the application for a waiver be submitted to the Treasury Secretary no later than 2-1/2 months after the close of the plan year. The applicant would have to alert each participant, beneficiary, and employee organization about the application for a waiver of minimum contribution requirements.

- Sets the formulas for minimum funding for single-employer defined benefit pension plans and phases in the threshold of what is considered a funding shortfall.

- Sets the funding target of a plan for any year as 100% of the current value of all liabilities attributable to participants and beneficiaries under the plan for that year (current law is 90%--and in some cases 80%). Deficits would have to be made up (i.e. "amortized") over seven years.

- Sets the valuation date for plans with greater than 500 participants as the first day of the plan year. If a plan has less than 500 participants, the plan could choose any day during the plan year as its valuation date.

- Directs the value of plan assets to be determined on the basis of any "reasonable" actuarial method of valuation that takes into account the fair market value of assets. Asset averaging could not cover more than three plan years and could not result in a valuation of averaged assets greater than 110% or lower than 90% of the fair market value of the plan's assets.

- In determining the value of liabilities under a plan for a plan year, liabilities attributable to benefits accrued as of the first day of the plan year would be taken into account. Any benefits which are expected to accrue during a plan year would not be taken into account (unless the plan is collectively bargained).

- In determining the value of liabilities under a plan for a plan year, the required interest rate would be that rate which, if used to determine the present value of the plan's liabilities, would result in an amount equal to the funding target of the plan for a plan year. The bill provides formulas for how this interest-rate calculation would be phased in over three years.

- Replaces the 30-year Treasury rate to measure pension liabilities with a three-tiered corporate bond yield curve (as detailed in the bill, phase-in beginning in 2007). The corporate bond yield curve is widely regarded as a more accurate tool.

- Requires that the probability of future benefit payments being made under the plan, including lump sums and other optional forms of benefits, be taken into account and included in the plan's funding target when determining the present value of a plan's liabilities.

- Provides special rules for "at-risk" plans (plans that are grossly underfunded—60% or less—and in danger of having to terminate)—including accelerated contribution requirements and increased penalties.

- Prohibits underfunded plans from using "credit balances" to replace required contributions.

- Imposes a lien on any plan for failures to make required contributions (in the amount of the unpaid contribution).

- Allows certain plan assets over 100% of a plan's funding target to be transferred to a qualified health benefits plan.

- Prohibits single-employer plans from offering benefits based solely on the occurrence of a plant shutdown or any other unpredictable contingent event.

- Prohibits the funding of executive compensation plans when pension plans of rank-and-file workers are significantly underfunded.

- Prohibits plans funded at less than 80% on the valuation date (subject to certain exceptions) from increasing the plan's liabilities by increasing benefits, establishing new benefits, changing the rate of benefit accrual, or changing the rate at which benefits become non-forfeitable.

- Prohibits lump sum distributions or any other accelerated form of benefits when a plan is funded at less than 80% on the valuation date (subject to certain exceptions).

- Prohibits all future benefit accruals for plans that are funded at less than 60% (after a plan's first five years).

- Requires that plan administrators provide written notice to plan participants and beneficiaries within 30 days after the plan has become subject to any of the above restrictions, subject to civil penalties.

- Inserts the above changes to ERISA into the tax code as well.

Title II: Funding Rules for [Multi-Employer] Defined Benefit Plans

- Establishes minimum funding standards for multi-employer pension plans.

- Directs every multi-employer plan to establish and maintain a funding standard account into which employer contributions can go and from which payments can be made.

- Provides procedures for the amortization of unfunded liabilities of plans using the account just described.

- Instructs plan actuaries to certify to the Secretary of the Treasury, within 90 days of the start of each plan year, whether a plan is in endangered or critical status for a plan year. A plan would be considered endangered if the plan has a funded liability percentage of less than 80% (and greater than 65%) or there is an equivalent projected deficiency in the any of the next seven plan years. A plan's status would be considered critical if the plan has a funded liability percentage of less than 65% or meets certain other tests (as detailed in the bill).

- If a certification of endangerment is filed, the plan sponsor has 30 days to alert participants, contributing employers, unions, the Secretary of Labor, and the Secretary of the Treasury. In addition, a funding improvement plan (as approved by all bargaining parties) would have to be filed within 240 days of the certification and would have to remove the plan from endangered status within ten years. While a funding improvement plan is being negotiated, no benefits could be increased in the plan. If no certification is filed, a plan will be assumed to be endangered.

- If a critical status certification is filed, the plan sponsor has 30 days to alert participants, contributing employers, unions, the Secretary of Labor, and the Secretary of the Treasury. In addition, a rehabilitation plan (as approved by all bargaining parties) would have to be filed within 240 days of the certification and would have to remove the plan from critical status (into endangered status or higher) within ten years. While a rehabilitation plan is being negotiated, no benefits could be increased in the plan. The bill limits the reductions in rates of future accruals that rehabilitation plans could implement. If no certification is filed, a plan will be assumed to be in critical condition.

- Levies a 5% surcharge (of the contribution otherwise required under the collective bargaining agreement) on each contributing employer for the first plan year in which a multi-employer plan is in critical status (10% for each subsequent year).

- Prohibits the trustees of a plan in critical status from reducing adjustable benefits of any participant or beneficiary in pay status at least one year before the first day of the first plan year in which the plan enters into critical status.

- Allows a plan sponsor to treat the failure of any contributing employer to make the required contributions under a rehabilitation plan as a partial or complete withdrawal by that contributing employer from the plan.

- Directs that—if a plan sponsor makes a determination that the plan will be insolvent in any of the next five plan years—the plan sponsor make an annual assessment of the current rehabilitation plan and take any allowable steps to ensure that the plan will not be insolvent in any of the subsequent five plan years.

- Repeals several provisions in ERISA regarding withdrawal liability (what companies owe multi-employer plans as the cost of withdrawing from the plan), including the provision limiting withdrawal liability payments to twenty years and the provision providing a special exemption from withdrawal liability for the long- and short-haul trucking industry.

- Provides that an employer who switches to contractor employees to do the same work that former employees (for who contributions to the plan used to be made) were doing incur partial or complete withdrawal liability from the plan.

- Allows certain plans covering employees in the building and construction industry to elect to adopt a rule under which an employer who withdraws from the plan in a complete or partial termination is not liable to the plan if the employer was a contributing employer for less than five years. *[The Education and the Workforce Committee reports that this rule is applicable to plans in other industries under current law.]*

- Inserts the above changes to ERISA into the tax code as well.

<u>Title III: Other Provisions</u>

- Provides for interest rate calculations regarding lump-sum distributions.

- Clarifies certain prohibited transaction rules.

- Provides for a 14-day correction period for certain transactions involving securities and commodities.

- Instructs the Government Accountability Office to report to Congress on the feasibility, advantages, and disadvantages of:
  --requiring an employee pension benefit plan to insure a portion of such plan's total investments;

--requiring an employee pension benefit plan to adhere to uniform solvency standards set by the Pension Benefit Guaranty Corporation that are similar to those applied on a state level in the insurance industry; and
--amortizing a single-employer defined benefit pension plan's shortfall amortization base over various periods of not more than seven years.

Title IV: Improvements in PBGC Guarantee Provisions

- Increases the annual insurance premiums paid by plans to the Pension Benefit Guaranty Corporation (PBGC). Plans funded below 80% would have a three-year phase-in of premium increases from the current $19 to $30 per participant per year. Plans funded at or above 80% would have a five-year phase-in from $19 to $30.

- Sets a special premium rate for certain terminated single-employer plans (excluding those terminated in bankruptcy reorganization—which must pay a $1,250 premium per participant for three years once they emerge from bankruptcy).

Title V: Disclosure

- Increases the disclosure requirements (to plan participants and the federal government) for defined benefit plan funding notices, including:
  --accelerating the due date;
  --requiring a statement of the ratio of inactive participants to active participants in the plan;
  --requiring an estimate of the value of plans assets and projected liabilities, as well as the plan's funded ratio;
  --requiring a summary of any funding improvement plan or rehabilitation;
  --making available copies of all actuary reports and financial reports received by the plan for a plan year; and
  --giving contributing employers (in multi-employer plans) the right to a notice of the amount of their withdrawal liability.

Title VI: Investment Advice

- Exempts from ERISA's and the tax code's prohibited transaction rules:
  --the provision of investment advice to a plan, its participants, or its beneficiaries;
  --the sale, acquisition, or holding of securities or other property pursuant to such investment advice; and
  --the direct or indirect receipt of fees or other compensation in connection with providing the advice.

- Allows pension plan administrators to provide voluntary investment advice to employees, as long as any potential conflicts of interest are disclosed. Fiduciary advisors—not employers—would be liable for any advice given.

- Adds the investment advice provisions to the tax code as well.

<u>Title VII: Benefit Accrual Standards</u>

- Clarifies the rules relating to the reduction in accrued benefits under ERISA, thereby creating a uniform age discrimination standard for all defined benefit plans. Specifically, a plan would not be treated as failing to meet ERISA requirements if a participant's entire accrued benefit would be equal to or greater than that of any similarly situated, younger individual (an individual identical in every respect, including period of service, compensation, position, date of hire, work history, and any other respect, <u>except</u> for age). Further, lump sum distributions would not be age discriminatory if such payment equals the worker's account balance or an accumulated percentage of the employee's final average compensation.

- Shields certain other practices regarding the accounting and adjustment of accrued benefits from being ERISA violations.

<u>Title VIII: Deduction Limitations</u>

- Increases the allowable tax deduction for contributions:
  --to single-employer plans (up to 150% of plan liabilities)
  --to multi-employer plans (up to 140% of plan liabilities).'

- In the case of employer contributions to one or more defined <u>contribution</u> plans, the tax deduction limit would only apply to the extent that such contributions exceed 6% of the compensation otherwise paid or accrued during the year to beneficiaries under the plan.

<u>Title IX: Enhanced Retirement Savings and Defined Contribution Plans</u>

- Makes permanent the retirement savings provisions of the Bush tax cut of 2001 (including the increased contribution limits for traditional IRAs and Roth IRAs). See Title IX of Public Law 107-16.

- Makes permanent the saver's tax credit (for certain retirement savings accounts set to expire at the end of 2006), which taxpayers could choose to have the IRS deposit directly to a savings account, IRA, or pension plan.

- Allows employers to implement an <u>automatic</u> enrollment plan for 401(k) (defined contribution) plans. Employees could affirmatively change their contribution election or opt-out altogether (after being informed in writing of these choices)—but otherwise would be deemed enrolled in the employer's automatic 401(k) program (which would not *have* to include existing employees). The automatic deferral of compensation could not exceed 10% and could not be less than:
  --3% during the first applicable plan year;
  --4% during the second year;
  --5% during the third year; and

--6% during and year thereafter.

At least 70% of eligible employees would have to participate in the program for it to qualify, and employers would have to match contributions in amounts up to 50% of elections.

- Allows active-duty servicemembers to make penalty-free early withdrawals from their retirement plans, as long as they've been activated for at least 179 days. This provision would apply only to distributions after September 11, 2001.

- Allows public safety employees in government plans to make certain penalty-free early withdrawals from their retirement plans.

- Allows combat zone compensation to be counted as gross income when determining the limitations on and deductibility of contributions to individual retirement plans. *[This would expand IRA eligibility for servicemembers.]*

- Directs the Treasury Secretary to produce a form allowing individuals to direct a portion of any tax refund directly to an individual retirement plan, beginning in 2007.

- Allows disabled people to contribute to an IRA, even if they do not have earned income.

- Allows the distributions from the retirement plans of deceased individuals to be rolled over tax-free into the retirement plans of non-spouse beneficiaries.

Title X: Provisions to Enhance Health Care Affordability

- Excludes from gross income the cash surrender value of a life insurance policy made as a payment for long-term care.

- Allows annuity contracts and life insurance contracts to include qualified long-term care insurance riders.

- Allows up to $500 in unused health benefits in flexible spending arrangements (FSAs) to be carried forward to the succeeding plan year.

- Allows public safety officers who retire or become disabled to make up to $5,000 of tax-free distributions annually from government pension plans to purchase health care or long-term care insurance.

Committee Action: On June 9, 2005, the bill was referred to the Education and the Workforce Committee (E&W) and the Ways and Means Committee (W&M). On June 22nd, E&W's Subcommittee on Employer-Employee Relations marked up and forwarded the bill to the full committee by voice vote. On June 30th, the E&W Committee marked up and ordered the bill reported to the full House by a vote of 27-0. On November 9th, the W&M Committee marked up, amended, and ordered the bill reported to the full House by a vote of 23-17.

Administration Position: A Statement of Administration Policy (SAP) is unavailable at this time but should become available before final passage of this bill. To read the SAP for the Senate's version of this bill (S. 1783), which is similar in many regards, visit this webpage: http://www.whitehouse.gov/omb/legislative/sap/109-1/hr1783sap-s.pdf

Cost to Taxpayers: CBO estimates that H.R. 2830, as reported by the Ways & Means Committee, would decrease mandatory spending by $116 million in FY2006, by $3.028 billion over the FY2006-FY2010 period, and by a net $305 million over the FY2006-FY2015 period. The bill would also decrease revenues by $155 million in FY2006, by $14.209 billion over the FY2006-FY2010 period, and by $71.828 billion over the FY2006-FY2015 period.

Does the Bill Expand the Size and Scope of the Federal Government?: While the bill would impose certain mandates on the private sector (see below), such mandates are in an arena of law in which the federal government is already heavily involved. Thus, this legislation would not increase the scope of the federal government. There is no indication that the size of the government would increase because of this bill.

Does the Bill Contain Any New State-Government, Local-Government, or Private-Sector Mandates?: CBO and the Joint Committee on Taxation report that the bill contains no intergovernmental mandates. However, the bill does contain private-sector mandates, as explained below in the CBO cost estimate:

> Some of the bill's changes to ERISA would impose mandates on sponsors and administrators of single-employer and multiemployer private-pension plans. CBO estimates that the direct cost to affected entities of the mandates in the bill, less the direct savings resulting from those mandates, would exceed the annual threshold specified in UMRA ($123 million in 2005, adjusted annually for inflation) in 2009 and thereafter. Most of that cost would result from the increase in premiums paid to the PBGC. JCT has determined that the tax provisions in the bill contain no private-sector mandates.

Constitutional Authority: The Ways & Means Committee, in House Report 109-232, Part 2, cites constitutional authority in Article I, Section 8, Clause 1 (the congressional power to lay and collect taxes, duties, imposts, and excises) and in the 16th Amendment (the congressional power to lay and collect taxes on incomes, from whatever source derived).

The Education and the Workforce Committee, in House Report 109-232, Part 1, cites constitutional authority in court cases regarding ERISA, which themselves cited Article I, Section 8, Clause 3 (the congressional power to regulate interstate commerce).

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