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STATEMENT OF KAREN FRIEDMAN
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ON THE
"PROTECTING EMPLOYEES AND RETIREES IN BUSINESS BANKRUPTCIES ACT OF 2007"
BEFORE THE SUBCOMMITTEE ON COMMERCIAL AND ADMINISTRATIVE LAW OF THE COMMITTEE ON THE JUDICIARY
U.S. HOUSE OF REPRESENTATIVES

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Madame Chairwoman, Members of the Subcommittee, thank you for the opportunity to testify today. I am Karen Friedman, Policy Director of the Pension Rights Center, a 32-year-old consumer rights organization dedicated to promoting and protecting the retirement security of workers, retirees, and their families.

In today's economic environment, where increasingly companies are restructuring and cutting benefits, it is more important than ever to provide strong safeguards for American families. I will focus my comments today on how corporate practices are affecting employees' and retirees' retirement security and discuss the important pension protections included in the "Protecting Employees and Retirees in Business Bankruptcies Act of 2007," (H.R. 3652).

H.R. 3652 will provide critical retirement protections to employees and retirees when their companies fail or restructure under the bankruptcy code. While companies once used bankruptcy proceedings only when they were truly in trouble, as a tool of last resort, they now commonly view bankruptcies as a viable business strategy that allows them to unfairly eliminate long-standing pension obligations to their workers and retirees.

United Airlines is a case study of how a giant corporation used the bankruptcy system to shed billions of dollars in pension obligations – leading to devastating and irreversible losses to tens of thousands of American families. By going into bankruptcy, United was able to transfer its pension liabilities to the Pension Benefit Guaranty Corporation (PBGC), the federal private pension insurance program. United then paid off its creditors, gave multimillion-dollar pay packages to its executives, and emerged profitable from bankruptcy. The losers were the hard-working middle-class flight attendants, mechanics, ticket agents, pilots, and other airline employees, whose pensions were reduced by $2 billion.

This corporate strategy is the subject of Fran Hawthorne's new book *Pension Dumping*, which traces how companies have moved from honoring pension promises as "sacrosanct, stronger perhaps than any other business contract," to viewing them as a burden they want to eliminate.

Hawthorne says that even companies that are reluctant to cut benefits are often forced to terminate the plan by so-called "vulture investors," who will only provide financing to a company if the pension obligations disappear.

While some of these companies emerge financially healthy – at least in the short-term – the workers and retirees often lose hundreds of thousands of dollars of the earned benefits that they were relying on to make it through retirement. In short, pension dumping is a short-term strategy with devastating long-term consequences.

The PBGC was created as a backstop to protect workers' pensions when companies go belly-up, in order to ensure that those who spent a lifetime working for a company would not lose their retirement security. And the majority of participants in terminated plans will, indeed, get all the benefits owed to them. But there are limitations created by Congress on how much the PBGC can guarantee. For instance, the PBGC pays a maximum age-65 benefit of $4,312.50 per month (or $51,750 annually) for plans terminated in 2008. This amount is adjusted for inflation every year. The agency, however, does not insure all the benefits on which workers' rely. The PBGC does not guarantee certain subsidized early retirement benefits or fully insure benefit improvements made within five years of a plan's termination, benefits that were gained in lieu of other compensation. In addition, under the most recent amendments to federal law, shutdown benefits, negotiated by unions, are now only partially guaranteed if the shutdown occurs within five years of the plan termination.

H.R. 3652 recognizes that many individuals are left without recourse when the PBGC only pays them partial benefits. This bill would enable active workers and retirees whose benefits are not fully insured by the PBGC to file a claim against the plan sponsor in bankruptcy court for the full amount they earned. Under current law, individual workers and retirees are precluded from making such a claim for the difference between what the PBGC provides and what the plan had promised.

This reasonable provision will make a world of difference to employees in hundreds of corporations and industries across the country, employees who meet their end of the bargain by working throughout their career with the promise of getting a pension based on all their years of work. Employees give up wage increases in exchange for the company contributing to the defined benefit pension plan on their behalf. When the pension plan is terminated – through no fault of their own – employees, in essence, experience a retroactive pay cut, losing benefits they earned and can never get back. And unlike other creditors who know they are taking risks in lending money to a corporation, workers – at least in the past – assumed their money was safe in the pension plan.

H.R. 3652 also includes provisions to ensure that executives cannot enrich themselves while employees suffer benefit cuts. The bill fairly provides that if an employer terminates a plan, the executive compensation arrangements must be discontinued as well. This provision would put an end to such unfair situations as when United CEO Glen Tilton, after the restructuring, paid himself $4.5 million in pension and other benefits – an astounding $25 million worth of stock and $6 million in stock options – not to mention his more than $3 million in salary and bonuses.[1]

[1] Hawthorne, Fran, *Pension Dumping: the Reasons, the Wreckage, the Stakes for Wall Street*, pp. 143-144 (2008)

It is unjustifiable for executives to pay themselves lavish compensation packages while terminating their employees' pension plan as well as reducing their salaries and other benefits.

Finally, the bill provides important protections to employees in 401(k) plans. At a time when defined benefit plans are being replaced by do-it-yourself savings plans, employees need to know that their money is protected. H.R. 3652 provides individuals with a new priority claim in bankruptcy court when the value of their company stock in a 401 (k) plan plummets because of corporate misdeeds or fraud. Enron is the most notorious example of such corporate abuse. Although Enron executives Ken Lay and Jeffrey Skilling were well aware the company was tanking, they persuaded their employees to continue to invest their 401(k) money in Enron stock – at the same time they were selling their own company stock. The ending of that sad story is well-known, as thousands of workers lost all their retirement money. But while the Enron collapse may have occurred six years ago, its lessons are still valid. Employees still are permitted to invest all their 401(k) money in company stock. If company executives breach their fiduciary duty by misleading individuals as to the value of that stock, then employees should have their day in court.

The Pension Rights Center thanks the Subcommittee for holding a hearing on this important bill that takes some important steps towards protecting American workers' and their families' retirement security. This bill recognizes that workers have upheld their end of their bargain – giving their labor and loyalty to companies – and at the very least they should have their day in court to protect what they have earned.