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October 16, 2002

Senator Max Baucus
Chairman, Senate Finance Committee
219 Dirksen Senate Office Building
Washington, DC 20510-6200

Senator Charles Grassley
Ranking Member, Senate Finance Committee
209 Dirksen Senate Office Building
Washington, DC 20510-6200

Senator Edward Kennedy
Chairman, Senate HELP Committee
644 Dirksen Senate Office Building
Washington, DC 20510-6300

Senator Judd Gregg
Ranking Member, Senate HELP Committee
835 Hart Senate Office Building
Washington, DC 20510-6300

Dear Senators Baucus, Grassley, Kennedy and Gregg:

We are writing to respond to a letter dated October 1, 2002 sent to you by the American Benefits Council. The ABC letter asserts that modest measures now under consideration for inclusion in the Senate "Enron" pension reform bill would "increase the costs, burdens and liabilities associated with sponsorship of retirement plans" to such an extent that they could lead employers to scale back their contributions or even abandon their plans. As appears in the enclosed memorandum, there is no basis for these claims.

ABC, which represents Fortune 500 companies and their consultants, appears to have lost sight of the fact that tens of thousands of hardworking Americans have lost billions of dollars in retirement savings as the direct result of shortcomings in the nation's private retirement laws. Unless meaningful reforms are included in the Senate bill, 401(k) catastrophes will continue to occur, jeopardizing the retirement security of countless other American workers.

The provisions that ABC objects to are compromises aimed at preventing Enron-type disasters from occurring in the future, and at helping individuals who lose money in these types of situations to recover their losses. They would also end a variety of pension inequities affecting homemakers, and provide a much-needed voice for workers' pension policy concerns within the federal government. At a time when employees' faith in Corporate America and confidence in their retirement security have plummeted to all-time lows, inclusion of these modest measures in the Senate bill will send a clear signal to American workers and their families that their policymakers are truly concerned about their future economic well-being.

Sincerely,

Karen W. Ferguson
Director

Karen D. Friedman
Director of Policy Strategies

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RESPONSE TO THE AMERICAN BENEFITS COUNCIL'S OCTOBER 1, 2002 LETTER TO SENATORS BAUCUS, GRASSLEY, KENNEDY AND GREGG

In a letter dated October 1, 2002, the American Benefits Council urged Senators Baucus, Grassley, Kennedy and Gregg to reject a series of reforms proposed for inclusion in upcoming Senate legislation aimed primarily at forestalling future Enron-type 401(k) catastrophes. In the letter ABC contended that, "Each provision individually would have significant repercussions. Cumulatively, these provisions… could lead employers to scale back their contributions to employee accounts," and even in some case conclude that sponsorship of a defined contribution plan is simply too expensive and risky." In fact, nothing contained in the proposed measures supports these claims.

- **Expanded ERISA Liability for Corporate "Insiders."** When corporate officials cause losses to 401(k) plan participants – for example, by deliberately misrepresenting the value of employer stock – it is important that courts be able to rule that the officials are personally liable to the participants. Otherwise, the employees may be entirely without recourse. Enron is a good example. Employees are currently suing Enron CEO Kenneth Lay alleging that he provided misinformation that led employees to invest their 401(k) money in Enron company stock. If Ken Lay can convince the court that he was not a "fiduciary" of the 401(k) plan, he could be let off the hook for employee 401(k) losses. The provision under consideration would clarify current law to ensure that company insiders are considered fiduciaries if their actions cause losses to 401(k) plans, and will provide an important deterrent to future wrongdoing by company executives. Contrary to ABC's contention, the provision will not result in "nuisance litigation." That is because under both the private pension law and federal court rules, lawyers who bring frivolous lawsuits are severely sanctioned by the courts, and are required to pay the attorney's fees and costs of the prevailing parties.

- **Mandatory Fiduciary Insurance.** Fiduciary insurance makes it possible for workers to get their money back when courts find that plan trustees have engaged in wrongful actions that have caused losses. Without this insurance, most employees who win lawsuits against 401(k) trustees will be able to recover very little, if anything, since the trustees are likely to have little in the way of personal assets. ABC contends that this insurance is inaccessible and costly. In fact, according to the companies that sell fiduciary insurance, it is widely available, and almost all large employers, and many smaller firms, already provide some level of insurance to protect plan trustees. Requiring fiduciary insurance is a win-win situation for both employees and trustees. The insurance ensures that employees will be made whole for their losses; and it protects the personal assets of trustees if they are sued and found liable for their actions. If, in fact, the cost of fiduciary insurance is going up for 401(k) plans holding excessive amounts of their own companies' stock, this is precisely why adequate insurance should be required. If insurance companies will only provide protection for plan officials who are managing prudently diversified portfolios, that will help ensure greater retirement security for workers. At the same time, the assurance of adequate insurance to protect against personal liability will encourage top-quality company officials to serve as fiduciaries.

- **Joint Trusteeship and Other Forms of Mandated Employee Representation.** Federal law imposes a duty of loyalty on pension trustees requiring them to act solely in the interests of plan participants' and beneficiaries. But, as workers at Enron and WorldCom discovered, when all of the trustees are company officials and the 401(k) plan allows investment in company stock, the officials are likely to be subject to acute conflicts of interest. If the value of the stock plummets, they will have an institutional interest in encouraging employees to continue to buy and to hold onto the company stock. Employee representation on 401(k) boards would provide a much-needed check on such conflicts. Contrary to ABC's suggestion that such representation would be a radical departure from current practice, joint trusteeship is already widespread in both the public and private sectors. In the $2.8 trillion public pension system, employees are represented on the boards of most funds. In the private sector, more than three thousand collectively bargained retirement plans are jointly administered. Both employer and employee trustees regularly receive training and professional advice. Moreover, the experience of the United Kingdom, which requires the election of "Member nominated trustees" to all retirement plans, including non-collectively bargained arrangements, demonstrates that trustee elections can be simple and inexpensive. Particularly in the case of 401(k) plans holding company stock, it is critical that employees have a say in the options that are available for the investment of their own retirement money.

- **Restrictions on Nonqualified Deferred Compensation.** The reform measures now under consideration recognize that nonqualified deferred compensation plans no longer warrant the tax-favored treatment they have been afforded. These plans permit companies to give generous tax breaks to company officials, without providing benefits to rank and file workers. Originally limited to small groups of executives at the very top of a company, and subject to forfeiture in the event of the company's bankruptcy, they have now been extended to a wide range of upper-middle (and sometimes even mid-level) managers, and are largely protected against losses. Proliferation of these plans in recent years has played a major role in the rollback of "qualified" pension plans, which provide benefits to workers at all income levels. Since companies can achieve their retirement compensation objectives for executives and managers through these "top hat" plans, they no longer need to provide benefits for them through "qualified" plans. As ABC notes, some smaller companies now offer only executive deferred compensation plans, and provide no plans for their other employees. The proposed reforms would restore to the Treasury the ability to address the tax and retirement policy problems raised by deferred compensation plans. (See "Well-Hidden Perk Means Big Money for Top Executives, *Wall Street Journal*, Ellen E. Schultz and Theo Francis, October 11, 2002, p. A1, for an in-depth discussion of these plans.)

- **Requirement for Annual Prudence Certification.** A requirement that plan fiduciaries certify once a year that the company stock offered to employees through their 401(k) plan is a prudent investment would serve an important educational purpose. Although ABC is correct, that federal regulations already subject fiduciaries to an ongoing duty to ascertain the prudence of holding employer stock, this provision would ensure that the "named fiduciary" of a plan (or the fiduciary responsible for determining plan investment options) undertakes a thoroughgoing review of the value of the stock at least once a year. This provision is a compromise that replaces stronger measures that would have provided much greater protection to employees by limiting the concentration of company stock in 401(k) plans. The provision could be significantly strengthened by also requiring the named fiduciary to certify that the plan's overall level of diversification is one that financial experts would deem prudent. As the Enron and WorldCom situations demonstrated all too painfully, the financial prospects of a company, and therefore the value of its stock, can change very quickly. No matter how much "accurate and adequate information" employees have about the stock, they will rarely be able respond rapidly enough to the changes. Since the only realistic protection against the vagaries of the stock market is for employees' investments to be prudently diversified, it would make sense for the fiduciary charged with acting solely in their interests to be required to advise them annually whether the plan's investments in the aggregate meet that test.

- **Mandated Spousal Consent and Automatic Survivor Benefits.** ABC completely mischaracterizes the important protections for homemakers in private retirement plans now under consideration. One of the provisions would study the feasibility of extending to 401(k)s and profit sharing plans a requirement that has existed for pension plans for nearly two decades (and that already applies to 401(k)s and profit sharing plans while an employee is working under the plan). This requirement would prevent employees who leave a plan from cashing out their retirement money without the consent of a spouse. Contrary to ABC's contention, if such a requirement were adopted, no plan would be required "to install a joint and survivor annuity." If a spouse did not consent to an early cash-out, the money would simply stay in the plan until retirement age when it would be paid out either as an annuity or as a stream of benefits. Also, this provision would only minimally impact 401(k) plan administration. These plans already are required to obtain spousal consent if a worker wants to designate someone other than a spouse to receive the account balance while he or she is working under the plan, and to provide forms to employees terminating employment. The only new records to be maintained would be the electronically scanned and stored signatures of those spouses consenting to cash-outs. The complaints cited by ABC of employees who do not want to get the consent of estranged spouses are no different from those rejected by Congress 18 years ago for traditional pensions. These employees can always file for divorce, and allow the state courts to apportion these retirement assets in an appropriate manner.

  ABC's objections to the second spousal provision are equally unwarranted. Rather than providing "automatic survivors benefits" as ABC claims, the provision would merely clarify an existing Treasury regulation that provides that, when divorce court orders are silent about the disposition of survivors benefits, decisions made by a couple to provide these benefits are preserved after a divorce, unless the employee subsequently makes the decision to cut off the benefits or give them to someone else. The provision is aimed at protecting lower-income women who cannot afford to hire lawyers knowledgeable about the complex legal requirements for preserving survivors benefits in divorce proceedings. ABC's cost and burden arguments have been addressed in a redraft of the provision.

- **Office of Pension Participant Advocate**. ABC objects to establishing an Office of Pension Participant Advocate within the Labor Department on the ground that such an office is "unnecessary," "duplicative," could result in the "development of divergent policies," and would be predisposed to litigation. In fact, such an Office is very necessary, would not duplicate the functions of any other office, would serve only in an advisory capacity, and would not litigate. The Office would serve as a voice for participants' policy concerns within the federal government, just as the Office of Advocacy within the Small Business Administration serves as a voice for small businesses. Such an office is urgently needed. Because of a fluke in the development of the private pension law, jurisdiction on private pension issues is split among three federal agencies. The Labor Department protects funds against mismanagement and helps individuals understand and enforce their rights, the Treasury makes sure that companies get tax breaks only if they follow the rules, and the Pension Benefit Guaranty Corporation pays benefits when underfunded defined benefit plans terminate. None of these agencies have a mandate to promote the pension policy concerns of individual workers. The Office of Pension Participant Advocacy would complement the work of the Pension and Welfare Benefits Administration's Office of Participant Assistance and Communications and Office of Research and Policy by hearing from employees about their policy concerns, documenting gaps in the laws affecting individuals, and developing reform recommendations for consideration by the agencies and Congress. The Office would also ensure that participants' interests are adequately represented in agency proceedings. At a time in our nation's history when employees and retirees are increasingly expressing an interest in exploring new approaches to improving and expanding our nation's private retirement programs, it is more important than ever that there be an office within in the federal government where they can turn.