November 2, 2005

Pension Reform Legislation Update

In July, the Senate Finance Committee approved the "NESTEG" pension reform legislation, including, among other things, far-reaching changes affecting cash balance plans and the funding rules applicable to single-employer pension plans. On September 8, the Senate Health, Education, Labor, and Pensions (HELP) Committee approved its own version of comprehensive funding reform and cash balance legislation, the Defined Benefit Security Act of 2005. Soon after, the leaders of the two committees, Finance Committee Chairman Charles Grassley (R-IA) and Ranking Member Max Baucus (D-MT) and HELP Committee Chairman Michael Enzi (R-WY) and Ranking Member Edward Kennedy (D-MA), negotiated a compromise pension reform bill that includes elements of the bills approved by the two committees. The compromise bill was introduced on September 28 as S. 1783, the Pension Security and Transparency Act.

In late September and early October, there was considerable momentum for the passage of pension reform legislation, in part because of the recent bankruptcy filings by Northwest Airlines and Delta Airlines. In fact, a "managers' amendment" to S. 1783 was being readied by the staff for the two committees and was slated for floor action the first week of October. However, efforts to bring the bill to the floor then bogged down, largely because of objections raised by Sens. Mike DeWine (R-OH) and Barbara Mikulski (D-MD), who proposed that the bill be amended to: (1) provide for the "smoothing" of asset values and interest rates used to calculate plan liabilities over a 3-year (instead of 12-month) period, and (2) base the applicability of the "at-risk liability" rules solely on whether the plan is under 60 percent funded -- not on the credit rating of the plan sponsor. Senators Grassley and Baucus in particular opposed the inclusion of the amendment in the bill because they felt it would undermine the compromise reached by the two committees. Thereafter, staff for Senate Majority Leader Bill Frist (R-TN) indicated that there may not be time to act upon the bill this year due to the large crush of pending business related to budget and appropriations bills, Hurricane Katrina, and Supreme Court nominations. It remains possible, however, that the dispute over the DeWine-Mikulski amendment – and any other issues that may have arisen since then – could be worked out and the Senate could pass the bill by "unanimous consent" later this year.

The House Education and the Workforce Committee approved its version of pension reform legislation (H.R. 2830, the Pension Protection Act) in June House Ways and Means Committee Chairman Thomas (R-CA) has indicated since early this year that his Committee plans to consider the pension funding reforms as part of a broader Social Security and retirement reform bill. The Committee has not yet marked up such a bill, and there have been various reports that the House leadership and Administration no longer plan to actively push Social Security reform this year. It is possible that the Ways and Means Committee will mark up H.R. 2830, as well as certain additional reforms related to defined contribution plans (e.g., auto enrollment provisions), some time in November.

Our side-by-side comparing key provisions in the introduced version of S. 1783 to H.R. 2830 as approved by the Education and the Workforce Committee is enclosed.

Meanwhile, House and Senate Committees have recently begun acting upon "budget reconciliation" legislation to make cuts in mandatory spending programs, including proposals to greatly increase premiums paid to the Pension Benefit Guaranty Corporation (PBGC). Under the budget rules, increases in PBGC premiums are scored as the equivalent of spending cuts because the increases reduce the potential exposure of the PBGC. The budget resolution approved by the House and Senate earlier this year generally calls for $35 billion in deficit reductions over 5 years, including (implicitly) through increases in PBGC premiums.

On October 18, the Senate HELP Committee approved a package of provisions that would:

- increase the single-employer flat rate premium from $19 to $46.75 per participant;
- increase the multiemployer premium from $2.60 to $8 per participant;
- index the single-employer flat rate and multiemployer premiums for inflation beginning in 2007; and
- impose a special premium of $1,250 per participant with respect to a company that terminates a plan in bankruptcy, with the premium payable for 3 years beginning after the company emerges from bankruptcy.

On October 26, the House Education and the Workforce Committee approved its own package of PBGC premium increases that would:

- increase the single-employer flat rate premium from $19 to $30 per participant and index it for inflation beginning in 2007;
- give PBGC discretion to increase the single-employer flat rate premium by up to 20 percent per year beginning in 2007, although Congress could adopt a joint resolution "disapproving" the increase; and
- impose a special premium of $1,250 per participant with respect to a company that terminates a plan in bankruptcy, with the premium payable for 3 years beginning after the company emerges from bankruptcy.

Both bills include language that would replace the premium increases contained in the budget reconciliation bill with alternative proposals included in the comprehensive pension reform legislation if such legislation is enacted before January 1, 2006. It is possible that the prospect of higher PBGC premiums – plus indications from key Congressional leaders that they will be reluctant to extend into 2006 the temporary replacement of the 30-year Treasury rate with a corporate rate for funding purposes – could spur action on comprehensive pension reform later this year.