[JOINT COMMITTEE PRINT]

DESCRIPTION OF S. 2105 and S. 2106

RELATING TO

STATE AND LOCAL PUBLIC EMPLOYEE BENEFIT PLANS: ADMINISTRATION OF EMPLOYEE BENEFIT PLANS

SCHEDULED FOR A HEARING

BEFORE THE

SUBCOMMITTEE ON SAVINGS, PENSIONS, AND INVESTMENT POLICY

OF THE

SENATE COMMITTEE ON FINANCE
ON MARCH 29, 1982

BY THE STAFF OF THE

JOINT COMMITTEE ON TAXATION

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INTRODUCTION

The Subcommittee on Savings, Pensions, and Investment Policy of the Senate Finance Committee has scheduled a public hearing on March 29, 1982, on S. 2105 and S. 2106 (introduced by Senator Chafee). The bills deal with the treatment of State and local public employee retirement systems, and would amend the Employee Retirement Income Security Act of 1974 (ERISA) relating to public employee retirement plans. In addition, S. 2105 would establish an Employee Benefit Administration, and would amend the Code as well as ERISA. The bills have been referred jointly to the Committee on Finance and the Committee on Labor and Human Resources.

This pamphlet is prepared by the staff of the Joint Committee on Taxation in connection with the Subcommittee's March 29 hearing. The first part of the pamphlet is an overview of public employee retirement systems and the scope of the bills. The second part is a summary of S. 2105 and S. 2106. The third part is an explanation of the provisions of the bills, including the relevant provisions of present law. Finally, part four is a statement regarding possible budget effects of the bills.

I. OVERVIEW

A. Background on State and Local Public Employee Retirement Systems

Financial status of plans

The 1977 Census of Governments counted 3,075 public employee retirement systems administered by State and local governments, distributed as follows (table 1):

TABLE 1.—NUMBER OF STATE-LOCAL PUBLIC EMPLOYEE RETIREMENT SYSTEMS IN 1977

Type	Number	Percent of total
State administered	197	6.4
Locally administered	2,878	93.6
Counties	165	5.4
Municipalities	2,420	78.7
Townships	194	6.3
School districts	83	2.7
Special districts	16	.5
Total	3,075	100.0

Source: 1977 Census of Governments, U.S. Bureau of the Census.

Several studies conducted since 1977 indicate that there now may be as many as 5,000 State and local government plans. They represent a major source of future retirement income for more than 9 million State and local government employees and dependents. Current benefits are paid to about 2.4 million persons.

In pension system reports to the Census Bureau for fiscal years that ended between July 1979 and June 1980, State and local government employee retirement systems reported annual receipts of $37.3 billion. Employee contributions accounted for 17 percent of that amount and investment earnings 36 percent; the rest—47 percent—were contributions from State and local governments (see table 2). Benefit payments and employee withdrawals of contributions amounted to $14 billion.

TABLE 2.—NATIONAL TOTALS OF STATE AND LOCAL PUBLIC EMPLOYEE RETIREMENT SYSTEM FINANCES, FISCAL YEAR 1980

[Millions of dollars]

Item	All public systems	State-administered systems	Locally administered systems		
			Total	Municipal	Other
Receipts	37,313	28,603	8,710	6,544	2,166
Employee contributions	6,466	5,285	1,180	751	429
Government contributions	17,532	13,010	4,521	3,558	963
From States	7,581	7,399	181	111	71
From local governments	9,951	5,611	4,340	3,447	893
Earnings on investments	13,315	10,308	3,008	2,234	774
Benefits and withdrawal payments	14,008	10,257	3,752	2,929	823
Benefits	12,207	8,809	3,399	2,698	701
Withdrawals	1,801	1,448	353	231	123
Cash and security holdings at end of fiscal year, total	185,226	144,682	40,544	29,992	10,552
Cash and deposits	4,220	2,647	1,572	932	640
Governmental securities	36,775	26,724	10,051	8,163	1,888
Federal	32,750	26,213	6,537	4,658	1,878
United States Treasury	17,520	13,814	3,706	2,613	1,093
Federal agency	15,230	12,399	2,831	2,045	786
State and local	4,025	511	3,514	3,505	9
Nongovernmental securities	144,232	115,311	28,921	20,897	8,024
Corporate bonds	75,037	60,871	14,166	9,879	4,287

TABLE 2.—NATIONAL TOTALS OF STATE AND LOCAL PUBLIC EMPLOYEE RETIREMENT SYSTEM FINANCES, FISCAL YEAR 1980—Continued

[Millions of dollars]

Item	All public systems	State-administered systems	Locally administered systems		
			Total	Municipal	Other
Corporate stocks	38,590	31,146	7,444	5,417	2,026
Mortgages	12,843	11,966	877	516	361
Other securities	16,238	10,677	5,561	4,615	946
Other investments	1,524	651	874	470	404

Note.—Because of rounding, detail may not add to totals.

Source: U.S. Bureau of the Census, "Finances of Employee Retirement Systems of State and Local Governments in 1970–80", p. 3.

At the end of fiscal year 1980, State and local pension systems held financial assets of $185.2 billion, as shown in table 2. Investment in nongovernmental securities amounted to $144.2 billion, or 79 percent, $36.8 billion in government securities, or 20 percent, and the rest was held in cash and deposits. The bulk of governmental securities held had been issued by the Federal Government, and the holdings were almost evenly divided between Treasury and federal agency issues. Bonds constituted more than half of the nongovernmental securities, and about one-quarter of the total were corporate securities. The rest of the assets were in mortgages and other securities and investments.

Administrative costs of the employee retirement systems have been excluded from these data because such costs primarily are met directly by the government involved, rather than by the retirement system as a separate entity. As a result, such data are not reported with other information concerning retirement systems.

Funding pension plans

State and local government employment increased at faster rates from 1950 through the 1970's than federal government or private sector employment. An inevitable association has been the expansion in the number and size of State and local government pension plans and in the costs and benefit payments. Inflation, greater labor mobility and earlier retirements, especially from public sector employment, have complicated the increasing burdens on public pension systems. A reasonable summary of the situation can be presented in a discussion of the decisions that must be faced in funding a pension system.

The objectives and limitations of the pension program must be defined first. Usually, public employee retirement benefits are based on the number of years of service, a measure of gross salary and a maximum benefit (ceiling) expressed as a percentage of the salary measure. Plans of this type are referred to as defined benefit plans. If liabilities under a defined benefit plan are to be funded in advance, estimates must be made with respect to such factors as the number of employees who will qualify for benefits, the salary levels upon which their benefits will be based, and their life expectancies (and those of their survivors). Also, estimates must be made as to the interest rates to be earned on plan assets.

An additional matter relates to inflation and cost-of-living adjustments that restore in full or part the loss in purchasing power. It is common for public pension plan contracts to provide for periodic adjustments, and those lacking a formal commitment often make such adjustments periodically by legislative action. If the inflationary adjustments have not been funded, cost-of-living adjustments conceivably could increase, or create, a plan's unfunded liability.

Funding a pension plan involves estimating the future time pattern of benefit payments and arranging a pattern of contributions to a fund which, with accumulated interest earnings, will be able to finance benefit payments. Alternatively, a pension fund may be established by a legislature that requires employee contributions at a specified percentage of payroll and annual appropriations that make up the difference between benefit payments and employee contributions; this is a pay-as-you-go system.

Most public defined benefit pension funds have unfunded liabilities on an actuarial basis. Recommendations to achieve full funding involve amortizing the estimated deficit over a period and reaching an equilibrium state of full funding thereafter. Failure to do so implies a pattern of pension costs which may increase at an increasing rate over time. Such a pattern may overburden an employer and may result in a curtailment of benefits.

Estimating the correction to be made involves estimating the levels and paths of several variables. The time pattern for the estimating period must project levels of employment, wages and salaries, real income, inflation, interest rates, average employment tenure, retirement age, and life expectancy of employees and dependents eligible for survivor benefits. Some of the variables are mutually reinforcing and others are offsetting. Different rates of change and time patterns of change also will produce mutually reinforcing and offsetting changes. The calculations of fully funded or unfunded liability are precise, but only after actuarial assumptions have been made about how the relevant variables will change in the future.

B. Scope of S. 2105 and S. 2106

In general

Under similar provisions of S. 2105 and S. 2106, the administrator of a public employee pension benefit plan would be required to meet reporting and disclosure standards. In addition, the bills would (1) prescribe a "prudent man standard" and other standards for fiduciaries of public plans, (2) prohibit certain transactions between fiduciaries and plans, and (3) require that fiduciaries of public plans be bonded. The provisions of the bills would be enforced by civil actions. A public plan would be subject to Federal standards except that, in some cases, plans would be exempt from Federal standards if State law provides for equivalent standards. The bills do not apply to Federal pension plans.

Under S. 2105, a public employee pension benefit plan that meets the reporting, disclosure, and fiduciary requirements of the bill would be treated as a qualified plan under the Internal Revenue Code. Also, S. 2105 would require that the President establish a new agency, the Employee Benefit Administration (EBA), to administer the provisions of the bill. The bill would generally transfer, from the Internal Revenue Service to the new agency, administration of the provisions of the Internal Revenue Code relating to qualified pension, profit-sharing, and stock bonus plans, to deferred compensation plans of State and local governments to certain health, legal, and fringe benefit plans, and to IRAs. The new agency would also administer the provisions of ERISA presently administered by the Department of Labor. The Pension Benefit Guaranty Corporation would also be transferred to the EBA.

Question of Federal authority

Questions have been raised as to Federal authority to regulate the employment practices of a State or local government with respect to its employees. Some commentators believe that the decision of the Supreme Court in *National League of Cities* v. *Usery* [1] indicates that Federal authority under the Commerce Clause of the Constitution does not extend to the regulation of State and local wage and benefit practices.[2] Others argue that the case has been interpreted narrowly by the Courts and that the provisions of the bill would withstand a constitutional challenge.[3]

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[1] 426 U.S. 833 (1976). In *National League of Cities,* the Supreme Court considered the 1974 amendments to the Fair Labor Standards Act under which minimum wage and maximum hour provisions of Federal law were generally extended to employees of States and their political subdivisions. In a 5–4 opinion, the Court held that the amendments were not within the authority granted to the Congress by the Commerce Clause. The Court held that the amendments would impair the State's ability to function effectively in a federal system and specified that the Congress may not exercise its power to regulate commerce so as to force directly upon the States its choices as to how essential decisions regarding the conduct of integral governmental functions are to be made.

[2] *State and Local Pension Systems—Federal Regulatory Issues,* Advisory Commission on Intergovernmental Relations, December 1980 (p. 5).

[3] See Pension Task Force Report on Public Employee Retirement Systems, Committee on Education and Labor of the House of Representatives, 95th Cong., 2nd Sess., March 15, 1970 (p. 17 et. seq.).

II. SUMMARY OF THE BILLS

Coverage

The bills (S. 2105 and S. 2106) would cover most public employee pension benefit plans maintained by any State or local government which provide retirement income to employees or which permit the employees to defer income for periods extending to, or beyond the termination of covered employment. The bills would not apply to public employee pension benefit plans maintained by the Federal Government or any agency or instrumentality thereof.

Reporting and Disclosure

S. 2105

The bill would require that a public employee pension benefit plan comply with reporting and disclosure standards. The standards would require that public plans file a registration statement identifying the plan, retain records, and establish a claims procedure. Pension plans would be required to publish a summary plan description and an annual report which includes a financial statement, an actuarial report, and, in some cases, a report from insurance companies from which the plan has purchased benefits. The reporting and disclosure rules would be administered by the Employee Benefits Administration (EBA), a new agency established by the bill. Plans required to meet equivalent standards under State law would be exempt from certain of the Federal requirements.

S. 2106

The bill is substantially the same as S. 2105, except that it would not establish an Employee Benefit Administration. Instead, the reporting and disclosure rules for public plans would be administered by the Secretary of Labor.

Fiduciary Responsibility

S. 2105

Under the bill, standards would be established for fiduciaries of pension plans for employees of State and local governments. The bill would also define certain acts of self-dealing as prohibited transactions.

The bill would require that covered plans be in writing and that all plan assets be held by a trust or by an insurance company. Under the bill, a public plan would generally be required to provide plan trustees with exclusive authority and discretion to manage and control plan assets. Bonding would be required for plan fiduciaries and certain plan employees.

All plan fiduciaries would be required to act in accordance with a "prudent man" standard. In addition, plan fiduciaries generally would be required to diversify plan investments (up to 10 percent of plan assets could be invested in qualifying employer securities, obligations, and real property), and would be required to act for the exclusive benefit of the plan participants and beneficiaries. Fiduciaries would be personally liable for losses sustained by a plan that result from violation of these rules.

The bill generally would prohibit a fiduciary (1) from dealing with the income or assets of a plan in his own interest or for his own account, (2) from acting in any transaction involving the plan on behalf of a person (or representing a party) whose interests are adverse to the interests of the plan or of its participants or beneficiaries, and (3) from receiving any consideration for his personal account from any party dealing with the plan in connection with a transaction involving plan assets. However, the bill would authorize the Employee Benefit Administration (EBA) to establish an administrative procedure for granting exemptions from the prohibited transaction rules and would also provide certain statutory exemptions.

S. 2106

The bill is substantially the same as S. 2105 with respect to fiduciary standards, except with respect to certain definitions of prohibited transactions and fiduciary duties and the limits on the acquisition of qualifying employer securities. Under S. 2106, prohibited transactions include certain transactions between a plan and a party-in-interest as well as acts of self-dealing by the fiduciary. Further, under certain circumstances, a fiduciary is made explicitly liable for breaches made by each co-fiduciary. The overall limit on acquisition of qualifying employer securities, etc. is reduced to five percent of plan assets.

Administration and Enforcement

S. 2105

Responsibility for administering the bill's provisions relating to public employee pension benefit plans would be assigned to the Employee Benefit Administration (EBA), a new Federal agency established by the bill. The EBA, State attorneys general, and other specified persons could bring civil actions against fiduciaries and plans to collect penalties and to otherwise enforce the provisions of the bill. Federal court jurisdiction is provided for the bill's fiduciary standards. Concurrent State and Federal jurisdiction is generally retained for other civil actions.

S. 2106

The bill is substantially the same as S. 2105, except that the bill would not establish an Employee Benefit Administration. Instead, the bill's provisions would be administered and enforced for the United States by the Secretary of Labor.

Tax-Qualification of Government Plans

Under S. 2105 only, the tax-qualification rules of the Internal Revenue Code for pension plans would not apply to public employee pension benefit plans. Instead, a public employee pension benefit plan which meets the requirements of the bill would be treated as a tax-qualified plan for all purposes under the Code. Accordingly, the Code's tax-qualification rules, including those prohibiting discrimination, limiting contributions or benefits, and defining prohibited transactions, would not apply.

Consolidation of Federal Administration

S. 2105

The bill would transfer to the new Employer Benefit Administration existing functions of the Departments of the Treasury and of Labor with respect to qualified pension, profit-sharing, and stock bonus plans, tax-sheltered annuities, tax-credit ESOPs, medical reimbursement plans, group legal plans, cafeteria plans, employee stock purchase plans, individual retirement accounts, deferred compensation plans for employees of State or local governments, voluntary employee beneficiary associations, supplemental unemployment benefit plans, employee-funded pension plans, and certain trusts established for payment of liabilities to multiemployer persion plans. Policymaking and other functions of the Secretaries of Labor and the Treasury under ERISA and the Internal Revenue Code would be transferred to the new agency. The EBA would have the authority to determine the status of pension, etc., plans under the tax laws, and to enforce ERISA standards by civil actions against plans and fiduciaries.

S. 2106

There is no provision under the bill to establish a new agency to administer pension, etc. plans. The bill's provisions relating to public employee pension benefit plans would be administered by the Labor Department. The Departments of the Treasury and of Labor and the Pension Benefit Guaranty Corporation would retain their respective responsibilities for administering and enforcing ERISA and those provisions of the Internal Revenue Code relating to employee benefit plans.

III. DESCRIPTION OF THE BILLS

A. Coverage

In general, the bills (S. 2105 and S. 2106) would apply to any public employee pension benefit plan (i.e., any plan, fund, or program maintained by a State or political subdivision thereof, or any agency or instrumentality of any State or political subdivision) which provides retirement income to employees or which permits employees to defer income for periods extending to or beyond the termination of covered employment. The bills would apply to defined contribution and defined benefit arrangements. However, the bills would not apply to plans maintained by the Federal Government or any agency or instrumentality thereof.

In addition, the bills would not apply to (1) employee benefit plans covered by ERISA; (2) unfunded excess benefit plans which provide benefits in excess of those permitted under qualified pension, etc., plans; (3) severance pay plans; (4) agreements to cover public employees under social security; (5) individual retirement accounts, annuities, or bonds (IRAs); (6) qualified cash or deferred arrangements; (7) tax-sheltered annuity programs; (8) eligible State deferred compensation plans; and (9) workers compensation and unemployment compensation plans.

B. Reporting and Disclosure

Present Law

The Internal Revenue Code requires every employer who maintains a pension, etc., or other funded plan of deferred compensation (whether or not tax-qualified) to file an annual return stating such information as is required under Treasury regulations with respect to the plan's (1) qualification, (2) financial condition, and (3) operations. The annual return is filed on the Form 5500 series.

The Code's requirement for an annual report applies with respect to a pension or retirement plan maintained by a State or local government.[1]

Explanation of Provisions

1. S. 2105

In general

The bill would establish the Employee Benefit Administration (EBA), a new agency. Generally, the administrator of a public employee pension benefit plan would be required to register the plan and file annual reports with the EBA. The registration statement would contain the name and address of the plan and of the plan administrator as well as any other information relating to the characteristics and identity of the plan that the EBA may require. Plans of a State or local government would be exempt from the Federal reporting and disclosure requirements if the governor of the State certifies that State law applies substantially equivalent requirements, that the State possesses adequate administrative capability, and that the State would collect annual reports and provide them to the Board.

Plan summary

The administrator of each plan covered under the bill would be required to publish a summary description of the plan and furnish a copy of the summary to each participant. Distribution of copies of material modifications and periodic updated summaries would also be required. Summaries of the plan and other information would be required to be written in a way that would be understood by the average plan participant and be sufficiently accurate and comprehensive to inform participants and beneficiaries of their rights and obligations.

The summary plan description would identify the plan, its administrators, and its trustees; describe the relevant collective bargaining provisions; refer to relevant Federal, State and local law;

[1] *State of California* v. *Blumenthal* 457 F. Supp. 1309 (D.C. Ca 1978).

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describe the rules governing eligibility requirements, vesting conditions, and disqualification or ineligibility for benefits; specify the procedures governing benefit claims and redress of claims, and provide certain other information.

Annual report

In general.—The Administrator of each plan would be required to publish an annual report for each plan year. The annual report would be filed with the EBA and furnished on request to plan participants and beneficiaries and other interested persons.

Separated participants with vested pension benefits.—The annual report would identify each plan participant who separated from service in the previous plan year with a vested right to a pension benefit and who neither returned to service during the plan year nor received a pension benefit during the plan year or the preceding plan year. The report would also include the nature, amount, and form of the benefit. Information filed on an annual report with respect to a separated plan participant would be forwarded by the EBA to the Social Security Administration.

The Social Security Administration would be required to maintain records of the public retirement plans in which individuals have vested benefits, and to provide this information to participants and beneficiaries on their request and also in response to their applications for social security benefits.

Financial report.—Financial statements in the annual report would be audited by an independent qualified public accountant who would present an opinion as to whether the statements conform with generally accepted accounting principles.[2] In preparing and certifying these reports, the independent qualified public accountant would not independently verify any actuarial data. Rather, the accountant would be required to rely on the correctness of any actuarial matter certified to by an enrolled actuary. The financial statements would provide detailed balance sheet data, as of the end of the plan year, and separate, comparative summary data for the plan year and the preceding plan year.

For the plan year, the balance sheet would provide a statement of year-end assets and liabilities and of changes in net assets available for plan benefits. These statements would include appropriate details of revenues, expenses and other changes aggregated separately by general source and application. Notes to the financial statements could provide information concerning significant changes in plan benefits and whether there were any significant changes in the plan affecting benefits; the funding policy and changes in it; and material relating to activities and transactions affecting the assets and liabilities.

Year-to-year comparative summaries would describe, in appropriately aggregated categories, assets and liabilities at their current value, and receipts and disbursements. Investment assets held

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[2] The Financial Accounting Standards Board has proposed to defer for 18 months the effective date of FASB Statement No. 35, "Accounting and Reporting by Defined Benefits Plans," for plans that are sponsored by state and local governmental units. In making its proposal for deferral, FASB noted that the Financial Accounting Foundation, which is responsible for organizing, funding and overseeing FASB, has agreed to organize a new governmental accounting standards setting body to replace the National Council on Governmental Accounting.

during a plan year would be described by information concerning the issuer, borrower, lessor, or other party to the transaction (including identification of a party in interest).[3] Also, the maturity date and value, rate of interest, cost and current value of each group of similar assets would be reported. However, where some or all of the assets of a plan or plans are held by an insurance carrier or a bank, the value of those assets would be certified by the insurance carrier or bank, and would not be audited by the independent qualified public accountant. In addition, detailed information would be required regarding each transaction entered into involving a person known to be a party in interest. The bill specifies information that would be required about all loans, fixed income obligations and leases that were in default or classified as uncollectable at the end of the plan year, with notation of cases where parties in interest are known to be involved. Alternative reporting requirements could be followed for investment assets placed in a trust.

Actuarial statement.—For a defined benefit plan, the annual report covering a plan year would include an actuarial statement prepared by an enrolled actuary. An actuarial valuation of the plan would be required every three years. An enrolled actuary would be required to rely on the correctness of any accounting matter with respect to which the independent qualified accountant has expressed an opinion.

The actuarial statement would show the total amount of contributions made or expected to be made for the plan year by the participants, employers and all others. In addition, previously unreported contributions received during the plan year that apply to preceding plan years would be reported. The report would show the estimated total covered compensation of active participants, as well as the number of active participants, terminated participants eligible for deferred vested pension benefits (or return of participant contributions), and all other participants and beneficiaries included in the most recent actuarial valuation. Included in the report would be the values, as of the most recent actuarial valuation, of the current assets accumulated in the plan, the amount of accumulated mandatory and voluntary contributions made for active participants, and specified details of the funding of the plan.

The bill also would require statements of the most recent computation of the actuarial present value of (1) all future plan benefits for active participants and terminated participants eligible for deferred vested benefits (or return of contributions), of (2) accumulated plan benefits for vested and nonvested active participants, of (3) total projected plan benefits, of (4) future covered compensation and of (5) the plan assets.

Insurance organization.—If some or all of the pension plan benefits are to be purchased from one or more insurance organizations, the annual report for the plan year would include a statement from the insuror with information on the premium rates or subscription charges paid; the total amount of premiums received, persons covered by each benefit class and total claims; dividends or

[3] The term "party in interest" refers to individuals and organizations employed by or providing services to the plan.

retroactive rate adjustments and selected other administrative details.

Information for participants, beneficiaries, et. al.

Within prescribed time limits, the administrator would furnish to each participant or beneficiary of the plan a copy of the summary description of the plan, and distribute to them information about amendments and modifications of the plan that may reasonably be expected to affect future benefits. Additional information or copies would be available on written request and at a reasonable charge.

Reports of benefit rights

Each participant or beneficiary would be entitled to receive annually the latest information available concerning the total accumulated plan benefits; the extent to which benefits are, or will, become vested; the earliest date on which the accumulated plan benefits may become vested; and the total accumulated contributions made by the participant, including any interest, under the terms of the plan. The information could be provided in the annual report or in a separate statement. Analogous information would be available to separated participants entitled to vested benefits. Each participant who requests would be furnished information about the alternative forms of benefits payments that would be available.

Filing with the EBA

The administrator of each public employee pension benefit plan would be required to file a copy of the annual report for the plan year with the EBA within 210 days after the close of the plan year. Additional relevent material also would be filed. The EBA would make the report and additional information available for inspection in the EBA's public document room. The EBA could reject what it determined to be an incomplete filing or a filing with any material qualification in the statement by an actuary or accountant. If a revised filing were not submitted within 45 days after the rejection, the EBA could, at the plan's expense, retain a qualified public accountant or enrolled actuary to perform an audit or prepare an actuarial report, or the EBA could bring a civil action to require an appropriate filing.

Records and documents that would be required to reconstruct or verify any information under these disclosure provisions would be required to be kept available for at least six years after the required filing date.

A review procedure would be required to provide full and fair review of an action that denies a claim for benefits.

Alternative methods of compliance; exemptions

The EBA could prescribe an alternative method of satisfying any of the requirements for reporting and disclosure if (1) the alternative method would provide adequate disclosure to participants and beneficiaries and adequate reporting to the EBA, and (2) the alternative method would decrease plan costs substantially or avoid unreasonable administrative burdens. The EBA also could exempt

any plan from meeting any of the reporting and disclosure requirements where necessary and appropriate in the public interest.

2. S. 2106

The requirements for reporting and disclosure by public employee pension benefit plans would be substantially the same as would be provided under S. 2105. Under S. 2106, however, the Secretary of Labor would be responsible for administering the provisions of the bill.

Effective Date

These provisions of the bills would be effective at the beginning of the second calendar year following the date of the submission of the report by the Advisory Council on Government plans.

C. Fiduciary Responsibility

Present Law

Under present law, a pension plan is a qualified plan if it meets the requirements of the Code Section 401(a). A trust forming a part of a qualified pension plan is also exempt from tax if certain requirements are met, including a requirement that, under the trust instrument, it is impossible, at any time before the satisfaction of all liabilities to employees and their beneficiaries, for any part of the corpus or income to be used or divested for purposes other than the exclusive benefit of employees or their beneficiaries. In addition, certain pension trusts, including a trust under a governmental plan,[1] are not exempt from taxation if they engage in any of the prohibited transactions provided by the Code (sec. 503(a) and (b)).

Under administrative rulings, an investment generally meets the "exclusive benefit" requirement of the Code if (1) the cost of the investment does not exceed fair market value, (2) a fair return commensurate with the prevailing rate is provided, (3) sufficient liquidity is maintained to permit distributions, and (4) the safeguards and diversity that a prudent investor would adhere to are present.

The Code (sec. 503) prohibits certain transactions between a plan and certain interested persons. The prohibited transactions include the lending of funds to certain interested persons without receipt of adequate security and a reasonable rate of interest, payment of excessive salaries, providing the trust's services on a preferential basis, substantial purchases or sales of property for other than adequate consideration, and engaging in any other transaction which results in a substantial diversion of trust assets. If the trust engages in any prohibited transaction, it loses its tax-exempt status for at least one year.

Interested persons include a person who creates, maintains, or makes a substantial contribution to the plan.

Explanation of Provisions

1. S. 2105

In general

The bill would establish rules for plan administration. It would also define certain acts of self-dealing as prohibited transactions.[2]

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[1] A governmental plan is a plan established and maintained for its employees by the Government of the United States, by any State or political subdivision thereof, or by any agency or instrumentality of any of the foregoing (sec. 414(d)).

[2] These rules are generally similar to the fiduciary and prohibited transactions rules made applicable to private employee plans by ERISA.

Under the bill, all plan fiduciaries would be required to act in accordance with a "prudent man" standard. In addition, plan fiduciaries generally would be required to diversify plan investments (with certain exceptions for plans that invest in qualifying employer securities) and must act for the exclusive benefit of the plan participants and beneficiaries. The bill would also require that all plans be in writing, that plan assets generally be held in trust, and that trustees generally have the exclusive authority to manage and control plan assets. However, asset management in certain circumstances could be delegated to qualified investment managers. The bill would also permit plan trustees to allocate their responsibilities if the plan so provides.

Fiduciaries would be personally liable for losses sustained by a plan that result from violation of these rules.

Plan administration

Establishment of the plan

Under the bill, every covered plan would be required to be established and maintained pursuant to written instruments. For this purpose, the term "instrument" would include a law of any State or political subdivision. The plan document would be required to provide for a named fiduciary who is to have authority to control and manage the plan operations and administration.

Plan contents

Under the bill, each plan would be required to state whether a funding policy or goal has been established for the plan. In addition, the funding policy or goal, the method of carrying out the policy, and the source of funds for the plan must be described in the plan.

The plan would be required to provide procedures for determining whether employer contributions are made in a timely fashion and for resolving any disputes as to the timing or amount of contributions.

With respect to benefits, the plan would be required to specify the criteria for eligibility, the applicable level of promised benefits, and the timing, form, and method of payment.

The bill would also require the plan to describe procedures for any allocation of duties relating to the operation and administration of the plan. Allocation and delegation of duties, including certain fiduciary duties (but not trustee duties), would be permitted only if the plan specifically provides for the allocation or delegation, and then only in accordance with the procedures established in the plan.

Each plan would also be required to provide a procedure for plan amendments and for identifying the persons who have authority to amend the plan (except to the extent that amendments are to be made by legislation). Additionally, a plan could provide that a person could serve in more than one fiduciary capacity under the plan, including service both as administrator and trustee. As described below, a plan could also provide for the hiring of advisors (including investment advisors) and investment managers.

Establishment of the trust

The bill provides that all plan assets are generally to be held in trust by trustees and also provides that the trustees would be required to manage and control the plan assets. In order that persons who act as trustees recognize their special responsibilities with respect to plan assets, trustees would be required to accept appointment before they act in this capacity.

If the plan provides that the trustees are subject to the direction of named fiduciaries, then the trustees would not have the exclusive management and control over the plan assets, but generally would be required to follow the directions of the named fiduciary. Accordingly, a plan could permit a fiduciary to appoint an investment manager. However, such investment manager would be considered a plan fiduciary.

A trust would not be required if plan assets consist solely of insurance contracts or policies issued by an insurance company qualified to do business in a State. Although these contracts need not be held in trust, the person who holds the contract would be considered a fiduciary and would be required to act in accordance with the fiduciary rules with respect to the contracts.

Exclusive benefit of employees

Under the bill, each fiduciary would be required to act solely in the interest of the plan's participants and beneficiaries. The bill would require that the assets of the plan be used exclusively to provide benefits to participants and beneficiaries or to pay reasonable plan administration costs. Therefore, the assets generally would not be permitted to inure to the benefit of the employer maintaining the plan. However, in the case of a contribution which is made by a mistake of fact or law, the bill would permit the contribution to be returned to the employer within one year after the administrator discovers the mistake.

Special asset rules

Plan assets

The bill provides rules defining the nature of plan assets. In the case of mutual funds and closed-end investment companies regulated by the Investment Company Act of 1940, the bill would not apply the fiduciary rules to the company merely because plans invest in their shares.

Similarly, the bill provides that the investment by a plan in insurance contracts or policies would not cause the assets of the insurer issuing the contracts to be considered plan assets, except to the extent that the assets are maintained by the insurer in one or more separate accounts (provided they do not represent surplus in any such account).

Transfer of assets outside the United States

The bill generally would prohibit a fiduciary from transferring or maintaining the indicia of ownership of any plan assets outside the jurisdiction of the district courts of the United States. Such a transaction could be permitted under regulations to be issued by the EBA.

Employer securities

Under the bill, a plan would not be permitted to acquire any employer securities other than qualifying employer securities, employer real property other than qualifying employer real property, or to make employer loans other than qualifying employer loans. Total plan investment in qualifying employer securities, qualifying real property, and qualifying loans would generally be limited to 10 percent of plan assets.

Under the bill, employer securities are defined as securities issued by an employer whose employees are covered by the plan, by an employer representative of such an employer, or by any affiliate of such employer of employer representative. Qualifying employer securities are defined as employer securities which are stocks or marketable obligations (including bonds, debentures, notes, certificates, and other evidences of indebtedness), provided such securities are traded on a national securities exchange or have a price otherwise established by independent persons. Securities would not be qualifying employer securities unless the plan holds no more than a quarter of the issue and independent persons hold at least one-half of the issue.

Employer real property is defined as real property leased by a plan to an employer whose employees are covered by the plan. Real property which is leased to an employer would be considered qualifying employer real property if each parcel of real property and the improvements on it are suitable (or adaptable without excessive cost) for more than one use and that where a plan holds more than three parcels of such property, the parcels are dispersed geographically. Investment in qualifying employer real property must also satisfy the usual diversification standards of the bill.

An employer loan is defined as a loan or other extension of credit (which does not constitute an employer security) between the plan and (1) the employer of employees covered by the plan, (2) an employer representative of such an employer, or (3) an affiliate of such employer or employer representative. Qualifying employer loans are employer loans bearing a reasonable rate of interest (i.e., a rate consistent with the fiduciary duties imposed by the bill) and fully secured by marketable securities.

Fiduciary duties

Prudent man standard

The bill would require that each fiduciary discharge his duties solely in the interest of participants and beneficiaries for the exclusive purpose of providing benefits to participants and beneficiaries and defraying reasonable expenses of plan administration. The bill would require a fiduciary to act with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in conducting an enterprise of like character and with like aims. In addition, a fiduciary would be required to diversify plan investments to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so. Plan fiduciaries would be required to act in accordance with the plan documents

and instruments to the extent that they are consistent with the statutory requirements imposed by the bill.

Certain individual account plans

Under the bill, a special rule is provided for individual account plans where the participant can exercise independent control over the assets in his individual account. In this case, the individual exercising control would be regarded as a fiduciary, and other persons who are fiduciaries with respect to the plan would not be held liable for any loss that results from the control by the participant or beneficiary. However, the investment could not contradict the terms of the plan, and if the plan on its face prohibits such investments, the fiduciary could not follow the instructions and thereby avoid liability.

Cofiduciary duties

Under the bill, if a plan so provides, named fiduciaries would be permitted to allocate their specific responsibilities among themselves, and named fiduciaries would be permitted to delegate all or part of their duties to others. Provided the allocation or designation does not violate the exclusive benefit or prudent man or diversification rules,[3] named fiduciaries would not be held liable for the acts or omissions of the persons to whom the duties have been properly allocated or delegated.

If the plan provides that a named fiduciary is to designate another person as a fiduciary to carry out a specific fiduciary activity, the named fiduciary would not be liable for any act or omission of that person in connection with the activity unless the designation or its continuation violates the exclusive benefit, the prudent man, or the diversification standards.

If assets of a pension plan are held by two or more trustees, the bill provides that each trustee is to use reasonable care to prevent any other trustee from breaching the fiduciary standards and that the trustees are to jointly manage and control the assets of the plan.

Prohibited transactions

Self-dealing

Under the bill, certain types of transactions between the plan and a party-in-interest would be specifically prohibited. Under these provisions, a fiduciary would be liable if he knew or should have known that he engaged in a prohibited transaction.

The bill generally would prohibit a fiduciary from dealing with the income or assets of a plan in his own interest or for his own account. However, this rule would not prohibit the fiduciary from dealings where he has an account in the plan and the dealings apply to all plan accounts without discrimination.

In addition, the bill would prohibit a fiduciary from acting in any transaction involving the plan on behalf of a person (or represent-

[3] Generally, in implementing the procedures of a plan, plan fiduciaries must act prudently and for the exclusive benefit of plan participants and beneficiaries. As a result, fiduciaries must act in this manner in choosing the person to whom they allocate or designate their duties.

ing a party) whose interests are adverse to the interests of the plan or of its participants or beneficiaries.

The bill would also prohibit a fiduciary from receiving any consideration for his own account from any party dealing with the plan in connection with a transaction involving the assets of the plan.

Administrative exemptions

Under the bill, the EBA would be authorized to grant a conditional or unconditional exemption from the prohibited transaction rules. An exemption could apply to any fiduciary or transaction, or class of fiduciaries or transactions, provided that the EBA determines (1) that such exemption is administratively feasible; (2) that the exemption is in the interests of the plan and of its participants and beneficiaries; and (3) that the exemption provides satisfactory safeguards to protect the rights of participants and beneficiaries.

Statutory exemptions

The bill would exempt the following transactions from the prohibited transaction rules:

(1) plan loans to participants or beneficiaries where such loans (a) are specifically permitted by the plan, (b) are available to all participants on a reasonably equivalent basis, (c) are not made available to certain highly compensated employees, officers or fiduciaries in an amount greater than the amount available to other employees, (d) are reasonably secured, and (e) bear a reasonable rate of interest;

(2) contracts or reasonable arrangements made with a party in interest for office space or legal, accounting, or other services necessary for the establishment or operation of the plan, provided no more than reasonable compensation is paid for these services.

(3) investment of all or a part of the plan's assets in deposits in a Federal or State-supervised bank or similar institution which is a fiduciary, provided certain requirements are met;

(4) provision of ancillary bank services by a bank or similar financial institution which is a fiduciary, if no more than reasonable compensation is charged for such services, if adequate internal safeguards are provided, and if the bank's action is in accordance with specific guidelines issued by the bank that will prevent the bank from providing ancillary services in an unreasonable or excessive manner or in a manner that would be inconsistent with the best interests of the plan's participants and beneficiaries;

(5) certain transactions between a plan and a common or collective trust fund or pooled investment funds maintained by a party-in-interest which is a Federal- or State-supervised bank or trust company, or a pooled investment fund of an insurance company qualified to do business in a State.[4]

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[4] To qualify for exemption, no more than reasonable compensation may be paid by the plan in the purchase (or sale), and no more than reasonable compensation may be paid by the plan for investment mangement by the pooled fund. Also, the transaction must be specifically provided for by the plan or by a plan fiduciary (other than the bank, etc., or its affiliates) who has authority to manage and control the plan assets.

Bonding

The bill generally would require every fiduciary of a public employee pension benefit plan (and every person who handles funds or other property of a plan) to be bonded. Generally, the amount of the bond would not be less than 10 percent of the funds handled and not less than $1,000 (nor more than $500,000, except that the EBA may prescribe an amount in excess of $500,000 which in no event may exceed 10 percent of the assets handled). The bill would not require a bond if plan benefits are paid only from the general assets of a union or employer. In addition, a bond would not be required for a domestic trust or insurance company subject to State or Federal supervision or examination if it has combined capital and surplus in excess of $1 million (or such other higher amount as determined by the EBA). However, a special rule is provided for banks or other financial institutions exercising trust powers if their deposits are not insured by the Federal Deposit Insurance Corporation. In this case, a bond will not be required if the corporation meets bonding (or similar requirements) of State law which the EBA determines are at least equivalent to bonding requirements imposed on banks under Federal law.

Civil liability

In general

A fiduciary who breaches the fiduciary requirements or prohibited transaction rules of the bill would be personally liable for any losses to the plan resulting from the breach. Such a fiduciary would also be required to restore to the plan any profits which he has made through the use of any plan asset. Also, such a fiduciary would be subject to other appropriate relief (including removal) as ordered by a court. (See also D. Administration and Enforcement, Explanation of Provisions—1. S. 2105, "Prohibited transactions.")

In addition, the bill would prohibit a person who is convicted of certain specified crimes from serving as a plan administrator, fiduciary, officer, trustee, custodian, counsel, agent, employee, or consultant of a plan for five years after conviction or five years after the date of imprisonment, whichever is later. However, such a person would be permitted to serve as an administrator, etc., of a plan if his citizenship rights have been fully restored or if the United States Board of Parole determines that his service would not be contrary to the purposes of the Act. An individual who is named a fiduciary in violation of this provision would be subject to removal.

A plan fiduciary would not be liable for any breach of fiduciary duty if it occurred before he became a fiduciary or after he was no longer a fiduciary. In addition, a legislator acting in his or her legislative capacity (or any person acting in a governmental capacity with respect to establishing a plan) would not be considered a fiduciary by reason of legislative actions taken in connection with a government plan.

Exculpatory provisions and liability insurance

Under the bill, exculpatory provisions which relieve a fiduciary from liability for breach of the fiduciary responsibility rules would be void and of no effect except that the fiduciary's ability to allo-

cate or delegate his responsibilities would not be affected. The bill also provides, however, that a plan may purchase insurance for itself and for its fiduciaries to cover liability or loss resulting from their acts or omissions. The bill would also permit a fiduciary to purchase insurance to cover his own liability, and permit an employer or union to purchase liability insurance for plan fiduciaries.

Limitation on actions

No action may be brought with respect to a fiduciary's breach of duty after the earlier of (1) six years after (A) the date of the last action which constituted a breach, or (B) in the case of an omission, the latest date on which the fiduciary could have cured the failure; or (2) three years after the plaintiff actually knows or had reason to know of the violation or omission (because of the filing of a report with the EBA). Additionally, where there is fraud or concealment, any such action may be brought not later than six years after the date of discovery.

2. S. 2106

Overview

S. 2106, like S. 2105, provides standards for plan administration, fiduciary duties, and prohibited transactions. Unlike S. 2105, however, it is the Secretary of Labor, rather than the EBA, who would be authorized to administer these provisions.

Plan administration

The provisions of the bill affecting plan administration are identical to those contained in S. 2105, except that this bill refers to fiduciary functions rather than duties and specifically defines fiduciary functions as any duty, obligation, power, authority, responsibility, right, privilege, activity, or program.

Special asset rules

The provisions of the bill defining plan assets are identical to those contained in S. 2105. The overall limitation with respect to acquisition of qualifying employer securities, other qualifying employer obligations, and qualifying employer real property, however, is five percent of plan assets (rather than 10 percent, as in S. 2105).

Fiduciary functions

The provisions of S. 2106 dealing with fiduciary functions differ from those of S. 2105 in the following respects:

(1) Under S. 2106, each fiduciary is made explicitly liable for breaches by any cofiduciary if the fiduciary participates in, or conceals an act or omission of the cofiduciary; if the fiduciary, by his own failure to act for the exclusive benefit of plan participants helps to create the cofiduciary's breach; or if such fiduciary has knowledge of a breach by a cofiduciary and fails to make reasonable efforts to correct the breach.

In addition, although S. 2106 permits allocation of fiduciary duties, each fiduciary who allocates or delegates duties is explicitly made liable for any act or omission by the person allocated or dele-

gated the duty if the fiduciary failed to act in a manner consistent with his fiduciary duties with respect to the actual allocation or designation, as well as the implementation or continuation of the allocation or designation. (Under S. 2105, the general requirement that a fiduciary act for the exclusive benefit of plan participants governs cofiduciary liability with respect to allocated duties.)

(2) Although S. 2106, like S. 2105, permits a plan to provide insurance for plan fiduciaries, S. 2106 would permit a plan to purchase such insurance only if the insurance permits recourse by the insurer against the fiduciary in case of a breach of fiduciary responsibility.

Prohibited transactions

The provisions of S. 2106 regarding administrative and statutory exceptions from the prohibited transaction rules are identical to those contained in S. 2105 (although administered by the Secretary of Labor rather the EBA). However, the definition of prohibited transactions in S. 2106 is broader. In addition to defining the self-dealing transactions of S. 2105 as prohibited transactions, the bill prohibits plan fiduciaries and parties in interest from engaging in additional specific transactions. Those transactions include: (a) the direct or indirect sale, exchange, or leasing of any property from the plan to a party in interest for less than adequate consideration (or from a party in interest to a plan for more than adequate consideration); (b) the direct or indirect lending of money or other extension of credit from a plan to a party in interest without the receipt of adequate security and a reasonable rate of interest (or from a party in interest to a plan with the provision of excessive security or unreasonable interest); (c) the direct or indirect furnishing of goods or services from a plan to a party in interest to a plan for more than adequate consideration); (d) transfer to, or use by or for the benefit of a party in interest, of any plan assets for less than adequate consideration; and (e) the acquisition of any employer security, employer real property, or employer loans in violation of the five-percent limit on qualifying securities, etc.

Effective Date

These provisions of the bills would be effective at the beginning of the second calendar year following the date of the submission of the report by the Advisory Council on Government Plans. (See D. Administration and Enforcement, Explanation of Provisions—1. S. 2105, "In general.")

D. Administration and Enforcement

Explanation of Provisions

1. S. 2105

In general

Responsibility for administering the provisions of the bill would be assigned to the Employee Benefit Administration (EBA), a new Federal agency established by the bill. The EBA would be empowered to prescribe regulations, conduct investigations, and enforce the bill's provisions by civil actions against fiduciaries, plan administrators, and others.

Under the bill, the EBA and other specified persons may bring actions to collect penalties assessed by the EBA or to otherwise enforce the bill's provisions. A penalty is imposed for a failure to file a required form with the EBA and a plan administrator could be liable for a court-imposed penalty for failing to provide requested information to a plan participant or other person entitled to the information under the bill.

Exclusive Federal court jurisdiction is provided for violations of the bill's fiduciary standards. Concurrent State and Federal jurisdiction is generally retained for other civil actions. If an individual plaintiff prevails in a civil action, the bill requires that the court award attorney's fees, unless certain requirements are met.

In addition, the bill would establish an Advisory Council on Government Plans. The Council is to establish voluntary guidelines for public employee pension benefit plans with respect to funding and vesting, and is directed to act in cooperation with affected employees, employers, employee organizations, and administrators.

Request for information

If the administrator of a public employee pension benefit plan fails or refuses to comply with a request for information to which (1) a plan participant, (2) a beneficiary of a plan participant, (3) an employee organization representing employees covered by the plan, or (4) a resident of State is entitled under the bill, then the person requesting the information could enforce the request by civil action.

In addition, where a plan administrator fails or refuses to comply with a request for information by mailing the requested information within 60 days, the court could find the plan administrator personally liable to the person making the request in an amount up to $100 a day from the date of the failure or refusal, or may order other appropriate relief. However, a plan administrator would not be personally liable for a failure or refusal to provide requested information, if the failure or refusal resulted from matters beyond the administrator's control.

Civil actions

The EBA or the attorney general of a State in which a public employee pension benefit plan is established could bring a civil action to collect a civil penalty or to recover from a fiduciary who breaches any of the duties imposed upon fiduciaries by the bill. The EBA or a State attorney general could also bring a civil action to enjoin an act or practice which violates a provision of the bill, or may seek other relief to redress the violation or to enforce the provision.

Plan participants, beneficiaries, and fiduciaries could also seek recovery from a plan fiduciary or otherwise enforce the bill's provisions by civil action. The EBA would have the right to intervene in any such action, or in any action brought by a State attorney general under the bill.

The bill provides that a public employee pension benefit plan may sue and be sued as a person. Any money judgment under the bill against a plan would be enforceable only against the plan as an entity, and not against any other person unless that person's liability is established in his or her individual capacity. In addition, the bill includes rules under which if a plan's summary plan description fails to designate an agent for service of legal process, service may be made upon the EBA. The agency would then be required to notify the plan administrator or any trustee of the pending action within 15 days after being served.

Failure to file a required form

In the case of a failure to file a required form with the EBA (for example, the annual report of a public employee pension benefit plan) on the date and in the manner prescribed, the person failing to file the form (in the case of the annual report, the plan administrator) would be liable for $10 for each day during which the failure to file continues. However, the total amount imposed for a failure to file could not exceed $5,000. The date on which a form would be required to be filed is to be determined without regard to any extension of time for filing, and a filing which is incomplete in any material respect could be considered a failure to file.

The penalty for a failure to file would be payable upon notice and demand by the EBA, and the EBA or the attorney general of a State in which the plan is established may bring a civil action to collect the penalty.

Information used for commercial solicitations

Under the bill, information filed with the EBA with respect to a public employee pension benefit plan could be provided to the public in computer-compatible form only after the person receiving the information declares that the information will not be used for commercial solicitations or similar purposes. Any person who files the required statement but uses the information for commercial purposes would be subject to a civil penalty not to exceed $5,000. The penalty is to be assessed by the EBA, and the EBA or the attorney general of a State in which the plan is established may bring a civil action to collect the penalty.

Prohibited transactions

The bill establishes a "two-tier" penalty system for prohibited transactions. If a party in interest with respect to a public employee pension benefit plan engages in a transaction with respect to the plan which is prohibited by the bill, the party in interest would be liable for an initial penalty not to exceed five percent of the amount involved. Generally, the amount involved in a prohibited transaction would be the amount of money or the fair market value of other property which is involved in the transaction. If the transaction were not corrected (in such matter and within such period as the EBA prescribes by regulation), the penalty could be increased to not more than 100 percent of the amount involved.

Under the bill, correcting a prohibited transaction would require undoing the transaction to the extent possible, but in any case placing the plan in a financial position not worse than it would have been in, if the party in interest had acted in accordance with the bill's fiduciary standards.

The penalty imposed upon a party in interest with respect to a prohibited transaction could be assessed by the EBA or by the attorney general of a State in which the plan is established. The EBA or the attorney general of the State could bring a civil action to collect the penalty.

Civil actions by a State attorney general

Notice to the EBA would generally be required before the attorney general of a State brings a civil action to collect a penalty or to otherwise enforce a provision of the bill. The attorney general may proceed with the suit only if the EBA does not, within 45 days after notice, indicate its intention to bring the action. However, no notice to the EBA would be required, and the attorney general could proceed without awaiting the agency's action, if the suit is brought under the provisions of a State law which is applied (pursuant to the governor's certification) in lieu of a corresponding provision of the bill.

Federal and State court jurisdiction

Under the bill, generally any civil action brought to collect a penalty, or to otherwise enforce a provision of the bill, could be brought either in a State court or a Federal district court. However, a civil action brought under the bill's fiduciary standards could be heard only in a Federal district court. Federal district courts would have jurisdiction of actions under the bill without regard to the amount in controversy or the citizenship of the parties.

Any action to review an order of the EBA, or to restrain or compel action by the agency, could be brought in a Federal district court where the EBA has its principal office, or in the Federal district court for the District of Columbia.

Attorney's fees

In any case in which a plaintiff plan participant, beneficiary or fiduciary prevails or substantially prevails in an action brought under a provision of the bill, the court generally would be required to award the plaintiff reasonable attorney's fees. However, an

award of attorney's fees would not be required if the court determines that the defendant acted in good faith and that the awarding of such fees would not further the purposes of the bill. In addition, the bill provides that a court could, in its discretion, award reasonable attorney's fees to a defendant who prevails or substantially prevails in an action brought under a provision of the bill.

Under these same rules, attorney's fees are to be awarded in cases brought under State or local law, if (pursuant to the governor's certification) State law is applied in lieu of applying a provision of the bill.

Effect upon State laws

The laws of State or local governments otherwise applicable with respect to public employee pension benefit plans would in every case be superseded to the extent of the bill provisions relating to (1) the management of plan assets, (2) fiduciary duties, (3) prohibited transactions, and (4) acquisitions of employer securities or employer real estate. The bill's remaining provisions would also supersede the otherwise applicable laws of State or local governments, except for those State laws which are to be applied (pursuant to the governor's certification) in lieu of a provision of the bill.

The provisions of the bill would not, however, relieve any person from any State law regulating insurance, banking or securities, and would not supersede any generally applicable criminal law of a State.

If a State or local law is applied (pursuant to a governor's certification) in lieu of applying a provision of the bill, the EBA generally could act to enforce the State law by civil action in a court of the State or in a Federal district court. In addition, in appropriate cases the EBA could assess civil penalties provided under the bill for violations of such a State or local law. Also, plan participants, beneficiaries, and fiduciaries could by civil action in a State court or Federal district court seek to enforce the provisions of such a State or local law, generally on the same basis as they could bring such an action to enforce a provision of the bill.

Interference with protected rights

It would be unlawful to interfere with the attainment of any rights to which a plan participant or beneficiary may become entitled under the bill, or to fire, fine, suspend, or otherwise discipline or discriminate against any participant or beneficiary for exercising any rights to which he or she would be entitled under the bill. A plan participant or beneficiary could bring a civil action against any person who interfered with his or her rights which are protected under the bill.

Advisory Council on Government Plans

The bill would require that an Advisory Council on Government Plans be established. The Council would consist of 11 members appointed by the President, generally for three-year terms. Not more than six members could be affiliated with the same political party, and the members would be representative of the employees, employee organizations, employers, and general public having a direct interest in public employee pension benefit plans.

Within one year after appointment of the Council's initial 11 members (the appointments would be required to be made within 120 days after the bill's enactment), the Council would be required to submit to the President and the Congress a report of its recommendations for implementing the bill's provisions. The Council could also recommend additional legislation.

The Council would be empowered to establish voluntary guidelines for public employee pension benefit plans with respect to matters for which requirements are not established by the bill (*e.g.*, vesting or funding). In addition, the Council would advise the EBA's Board of Directors with respect to carrying out the agency's functions with respect to public employee pension benefit plans.

2. S. 2106

The administration and enforcement provisions in S. 2106 (title III of the bill) generally parallel those of S. 2105. However, S. 2106 does not provide for the establishment of the EBA as an independent Federal agency. Accordingly, under S. 2106 the Secretary of Labor would be responsible for administering and enforcing the bill's provisions relating to public employee pension benefit plans.

In addition, under S. 2106 the law of a State or local government would be applied in lieu of applying a provision of the bill upon certification by the Secretary of Labor, rather than by the governor of the State.

Effective Dates

The provisions authorizing the creation and administration of the Advisory Council on Governmental Plans would be effective as of enactment. The provisions (under S. 2105) authorizing the EBA to issue regulations would be effective on the date the Council submits its advisory report. The remaining provisions would be effective at the beginning of the second calendar year following the date of the submission of the report by the Advisory Council on Governmental Plans.

E. Tax Qualification of Government Plans

Present Law

Under present law, a funded pension plan, including a governmental plan,[1] is a qualified plan if it meets certain requirements of the Internal Revenue Code. Also, a trust forming a part of a qualified pension plan is exempt from tax as a qualified trust if (1) employer contributions to the trust are made for the purpose of distributing the corpus and income to employees and their beneficiaries, and (2) under the trust instruments it is impossible for any part of the trust corpus or income to be used for, or diverted to, purposes other than the exclusive benefit of employees before the liabilities to employees and their beneficiaries are satisfied. In addition to other tax-qualification requirements, the plan must not discriminate in coverage or in contributions or benefits in favor of employees who are shareholders, officers or highly compensated. Also, contributions or benefits must not exceed specified limits.

The Internal Revenue Service has announced that issues concerning prohibited discrimination in coverage or in contributions or benefits under government plans will not be raised by the Service until a review of the antidiscrimination rules is completed.[2] The Service announced that it is reconsidering the application of the antidiscrimination rules to plans covering elected and appointed officials of State and local governments. Pending completion of its review, the Service will resolve any issue under the rules in favor of a government plan's retaining its tax-qualified status.

Under present law, a trust forming a part of a government plan is not exempt from tax if the trust engages in any of the prohibited transactions provided by the Code.

Explanation of Provisions

1. S. 2105

A trust forming part of a public employee pension benefit plan which meets the requirements of the bill would be treated as a tax-qualified trust for all purposes of the Internal Revenue Code. It is intended if a trust is treated as tax-qualified, plan of which the trust is a part would also be treated as tax-qualified. Accordingly, the Code's tax-qualification rules otherwise applicable with respect to government and other funded pension plans, including those prohibiting discrimination and limiting contributions and benefits, would not apply.

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[1] A government plan is a plan established and maintained for its employees by the Government of the United States, by any State or political subdivision thereof, or by any agency or instrumentality of any of the foregoing.

[2] I.R.S. News Release IR-1869, August 10, 1977.

Benefits paid from a trust under a public employee pension benefit plan which meets the requirements of the bill would be entitled to the favorable tax treatment accorded benefits paid under tax-qualified plans. Therefore, benefits distributed as a lump sum distribution would be accorded special 10-year forward income averaging treatment, or could be rolled over, tax-free, to another qualified plan (whether of a private employer or another public employer) or to an individual retirement account, annuity or bond (IRA). Also, certain estate tax and gift tax exclusions would apply.

The bill also would add a new provision to the Code which would exempt from tax a trust forming a part of a public employee pension benefit plan which satisfies the bill's requirements. In the case of a trust exempt from tax under the new provision, the prohibited transaction rules of the Code would not apply.

Under the bill, the EBA would determine whether a public employee pension benefit plan satisfies the requirements of the bill, and whether a related trust is exempt from tax. The EBA would inform the Internal Revenue Service of its determination.

2. S. 2106

S. 2106 does not provide for the establishment of the Employee Benefit Administration (EBA). In addition, present-law rules relating to the tax qualification of governmental plans and the tax exemption of related trusts would continue to apply. Responsibility for administering the rules would remain with the Secretary of the Treasury.

Effective Date

These provisions of the bills would be effective at the beginning of the second calendar year following the date of the submission of the report by the Advisory Council on Government plans.

F. Employee Benefit Administration

Background and Present Law

Background

Generally, under pre-ERISA law, the Internal Revenue Service was responsible for administering provisions of the tax law providing favorable tax treatment for pension plans, profit-sharing plans, stock bonus plans, trusts under those plans, plan participants (or their beneficiaries), and employers who maintain plans.

If a pension, etc., plan qualifies under the tax law then, under ERISA and prior law, (1) a trust under the plan is generally exempt from income tax, (2) employers are generally allowed deductions (within limits) for plan contributions for the year the contributions are made, even though participants are generally not taxed on plan benefits derived from employer contributions until the benefits are distributed, (3) benefits distributed as a lump sum distribution are accorded special capital gain and 10-year income averaging treatment (and, under ERISA, may generally be "rolled over" tax-free to an individual retirement account or another qualified plan), and (4) certain estate and gift tax exclusions are provided.

Under ERISA and prior law, a trust qualifies if (1) employer contributions to the trust are made for the purpose of distributing the corpus and income of the trust to employees and their beneficiaries, (2) under the trust instrument, it is impossible for any part of the trust corpus or income to be used for, or diverted to, purposes other than the exclusive benefit of employees at any time before its liabilities to employees and their beneficiaries are satisfied, and (3) the trust is part of a plan which qualifies under the tax law.

Under ERISA and prior law, tax-qualified pension, etc., plans are required to satisfy tests designed to assure that they cover employees in general, rather than merely those employees who are officers, share-holders, or highly compensated.

Under pre-ERISA standards a pension, etc., trust lost its income tax exemption (and the plan of which it was a part generally lost qualification under the "exclusive benefit" rule) if it engaged in certain types of self-dealing transactions with anyone who was a creator of the trust or a substantial contributor to the trust, or with certain related persons, unless the transaction met an "arms's-length" test. ERISA provides a list of specific prohibitions, violations of which result in sanctions against the self-dealers rather than against the trusts or plans.

Under ERISA and prior law, trusts under qualified pension, etc., plans are subject to the tax imposed on unrelated business taxable income.

Under the tax provisions of ERISA and prior law, a plan covering an owner-employee [1] (an H.R. 10, or Keogh, plan) is required to meet special standards relating, for example, to the group of employees covered by the plan, pre-retirement vesting, plan fiduciaries, and the time benefits are distributed. Contributions on behalf of any self-employed individual are limited in terms of the individual's net earnings from self-employment, as defined for purposes of the tax on self-employment income with certain modifications.

Under pre-ERISA law, an employee covered by a pension, etc., plan which did not qualify under the tax law could not compel compliance with the qualification standards of the tax law—the employee's rights under the plan were determined under local law on the basis of plan provisions. Noncompliance with the tax standards resulted in loss or denial of the plan's tax qualification (and a loss or denial of the tax exemption for a trust forming a part of the plan).

Under pre-ERISA law, the Welfare and Pension Plans Disclosure Act (WPPDA) required reporting and disclosure by administrators of both welfare and pension, etc., plans. However, the WPPDA exempted any plan covering fewer than 26 participants and plans administered by tax-exempt fraternal benefit societies or tax-exempt charitable, educational, religious, or civic organizations.

In addition to filing with the Department of Labor, under the WPPDA plan administrators had to make copies of filings available for inspection by any participant or beneficiary at the plan's principal office and, upon written request by a participant or beneficiary, furnish a copy of the plan description and an adequate summary of the latest annual report.

Pension, etc., trusts under ERISA

In general

Generally, ERISA preserved the plan and trust qualification standards prescribed by prior law, established additional qualification standards, and provided minimum standards for pension, etc., plans which, if violated could result in tax sanctions as well as non-tax civil and criminal sanctions and injunctive relief to compel compliance. Also, ERISA preempted the regulation of most private pension, etc., and welfare plans by the States.

Reorganization Plan No. 4

Responsibility for administering and enforcing the provisions of ERISA is generally assigned to the Department of the Treasury and the Department of Labor.[2] Under ERISA, both Departments have authority to issue regulations, rulings, and opinions, and in some cases grant variances and waivers from ERISA standards. This shared jurisdiction under ERISA was the subject of Reorgani-

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[1] An owner-employee is one who owns a trade or business as a sole proprietor or is a partner who owns more than a 10-percent interest in a partnership which operates a trade or business.

[2] Responsibility for administering the pension plan termination insurance provisions of ERISA is assigned to the Pension Benefit Guaranty Corporation, a corporation within the Department of Labor. The Joint Board for the enrollment of actuaries establishes standards and qualifications for enrolled actuaries. The United States Tax Court has jurisdiction to issue declaratory judgments in some cases with respect to the qualified status of pension, etc., plans.

zation Plan No. 4 of 1978.[3] The plan largely eliminates the overlapping authority of the Department of the Treasury and the Department of Labor to promulgate regulations, rulings and opinions, or to grant variances or waivers. However, both Departments retain their separate enforcement powers. Thus, the Reorganization Plan continues the Treasury's authority to audit plans and levy tax penalties for any deviation from the Code's standards. The plan also continues the authority of the Department of Labor to enforce ERISA standards by civil action against plans and fiduciaries.

Under the Reorganization Plan, the Treasury generally has authority for the minimum standards of ERISA and prior law. Thus, it is generally the responsibility of the Internal Revenue Service to issue regulations, rulings or opinions, or grant variances or waivers, with respect to funding, plan participation, and vesting and accrual of benefit rights. The Department of Labor generally is responsible for the administration of ERISA's reporting, disclosure, and fiduciary standards and prohibited transaction rules.

Minimum age and service standards

Under the minimum age and service standards of ERISA, a pension, etc., plan generally cannot exclude an employee from plan participation on the basis of age or length of service if the employee has attained age 25 and completed one year of service. Generally, a year of service consists of 1,000 hours of service within a designated 12-month period.

The minimum age and service standards are tax-qualification standards for plans; accordingly, they are administered by the Internal Revenue Service. The non-Code provisions of ERISA also require compliance with these standards by qualified and most nonqualified pension, etc., plans; accordingly, the minimum age and service standards are also enforced by the Labor Department.

Coverage standards

Since 1942, the tax law has explicitly required that qualified plans cover employees in general rather than merely an employer's key employees. A plan satisfies the coverage rule if (1) it benefits a classification of employees that does not discriminate in favor of employees who are officers, shareholders, or highly compensated, or (2) the plan benefits a prescribed percentage of the employees.

In applying the percentage rule under ERISA, however, only those employees who have satisfied the plan's minimum age and service requirements are taken into account. In addition, in applying either the classification or percentage tests under ERISA, em-

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[3] The Reorganization Act of 1977 (Public Law 95–17) extended for three years the authority of the President to submit plans to Congress proposing the reorganization of agencies in the Executive Branch. Under this Act, a reorganization plan takes effect 60 days after transmittal to the Congress unless either House of Congress passes an unfavorable resolution.

The intent of the Reorganization Act is to give the President the ability to reorganize the means by which the Executive Branch administers the law, not the substantive content of the programs it administers.

ployees covered by an agreement which the Labor Department finds to be a collective bargaining agreement may be excluded from consideration if the Internal Revenue Service finds that retirement benefits were the subject of good faith bargaining.[4]

Neither the minimum age and service standard nor the coverage standard applies to a governmental plan, a church plan, a plan established by a tax-exempt society, order, or association (described in sec. 501(c) (8) or (9) or certain plans not providing for employer contributions. In addition, the nontax minimum age and service standards do not apply to certain tax-exempt pension trusts under plans funded solely by employee contributions. Plans exempted from the ERISA minimum age and service standards and coverage standards are required to meet the pre-ERISA coverage standards of the tax law in order to be tax-qualified.

Vesting standards—percentage schedules

ERISA established three alternate vesting schedules under which the nonforfeitable percentage of an employee's benefit derived from employer contributions [5] depends, in whole or in part, upon the number of years of service the employee has completed. As under the minimum service standard, a year of service generally consists of at least 1,000 hours of service within a designated 12-month period. In addition, the Internal Revenue Service may require more rapid vesting, in certain circumstances, in order to prevent discrimination by a qualified plan in favor of employees who are officers, shareholders, or highly compensated.

Generally, administration under the vesting standards follows the same pattern as that under the minimum age and service standards. Accordingly, the authority to prescribe regulations under the vesting standards is generally assigned to the Treasury Department, and the authority to define an hour of service by regulation is assigned to the Labor Department. In addition, the Labor Department has exclusive authority to prescribe regulations under rules permitting a suspension of benefit payments where a former employee is reemployed.

The vesting standards are administered by the Internal Revenue Service in connection with the qualification of a plan or trust under the tax laws. The vesting standards (other then the rules relating to prohibited discrimination) are also a part of the non-Code law enforced by the Labor Department. Under the non-Code law, the vesting standards apply to qualified and most nonqualified plans.

Vesting standards—accrued benefit standards

In addition to providing minimum standards for the nonforfeitable percentage of an employee's benefit accrued under a plan, ERISA provides minimum standards for the accrued benefit to which that percentage is applied. The rate at which an employee

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[4] Other exclusions are provided (1) in the case of plans established or maintained pursuant to collective bargaining agreements (determined by the Labor Department) between airline pilots and employers, and (2) for nonresident alien employees who receive no earned income (defined by sec. 911(b)) from the employer which is income from sources within the United States (defined by sec.861(a)(3)).

[5] All benefits derived from employee contributions are required to be nonforfeitable.

accrues benefits under a defined benefit plan [6] is tested, under the accrued benefit standards of ERISA, on the basis of the number of years the employee has been a plan participant.

Generally, authority to prescribe regulations under the accrued benefit standards is assigned to the Treasury Department. Enforcement authority is assigned in the same manner as under the vesting standards (the rules enforced by the Labor Department generally apply to qualified and to most nonqualified plans).

Funding standards

Under ERISA, pension plans are required to satisfy minimum funding standards.[7]

Amounts required to be contributed to a qualified plan under the funding standards are generally deductible. Authority to prescribe regulations under the funding standards is generally assigned to the Treasury Department. Under Reorganization Plan No. 4, the Treasury Department also prescribes the rules under which retroactive amendments may be approved or amortization periods may be extended.

Under the Internal Revenue Code, the funding standards are enforced by application of an excise tax on funding deficiencies. Generally, failure to satisfy the funding standards does not result in the disqualification of a pension plan.[8] The funding standards are also a part of the non-Code law enforced by the Department of Labor (the non-Code rules apply to qualified and most nonqualified plans).

Limits on benefits and contributions

In order to limit the extent to which individuals can use tax-favored arrangements to provide for retirement, the Code provides overall limits on benefits and contributions under qualified pension, etc., plans, tax-sheltered annuities, simplified employee pensions, or any combination of these arrangements. The limitation for an individual under a tax-favored retirement arrangement is based, in part, upon the individual's compensation. In the case of a self-employed individual, the limitations are generally based upon net earnings from self-employment. Special limitations apply to employee stock ownership plans (ESOPs). Under the limitation rules, benefits and contributions for an individual under plans of related employers are aggregated.

No equivalent rules are provided under the non-Code provisions of ERISA.

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[6] Generally, a defined benefit plan provides a specified benefit level (e.g., as under the Federal civil service pension plan). Defined contribution plans, in contrast, are plans under which separate accounts are maintained for plan contributions allocated to each employee, and an employee's accrued benefit depends solely upon the balance of his or her separate account (e.g., as in a profit-sharing plan).

[7] The standards apply to defined benefit pension plans because those plans promise a specified benefit (for which funding is required), and to pension plans which promise a fixed or determinable contribution rate. The Internal Revenue Service may waive the standard for up to 5 out of 15 years, but the waived contributions must be made up in subsequent years.

[8] Church plans which have not elected to be covered by ERISA and governmental plans are not subject to the ERISA funding standard. Accordingly, they remain subject to prior law under which a plan does not qualify unless it provides full vesting of benefits (to the extent the benefits are funded) in the event of a complete discontinuance of contributions.

Plans for self-employed individuals and shareholder-employees

The Code permits a self-employed individual who operates a trade or business to enjoy the benefits of a tax-qualified plan if the plan meets special additional standards. In addition, contributions to a defined contribution plan on behalf of a self-employed individual are limited to the lesser of $15,000 or 15 percent of the individual's net earnings from self-employment. Under rules applicable to electing small business corporations (subchapter S corporations), if contributions on behalf of a shareholder-employee [9] exceed the $15,000/15-percent limit under a defined contribution plan, the excess is taxed to the shareholder-employee. The Code also provides for defined benefit H.R. 10 plans and subchapter S plans. In addition, H.R. 10 plans and plans of subchapter S corporations are subject to the overall limits on benefits and contributions applicable to other qualified plans.

No equivalent rules are provided under the non-Code provisions of ERISA.

Individual retirement accounts (IRAs) etc.

Within limitations, the Code allows a deduction for an individual's contributions to an individual retirement account (IRA). The deduction is not to exceed the lesser of (1) 100 percent of the individual's compensation includible in gross income (including self-employment income), or (2) $2,000 ($2,250 in the case of certain IRAs covering an individual and spouse).

A lump sum distribution from a qualified plan can be "rolled over" tax-free to an IRA. If an individual engages in prohibited self-dealing with an IRA, the account is disqualified and amounts held in the account are taxed to the individual.

The Code also allows plan participants a deduction for qualified voluntary employee contributions to a qualified plan, government plan, or tax-sheltered annuity program. The deduction allowed an individual for the contributions is in lieu of the deduction allowed for IRA contributions, and is generally subject to the same limitations.

No equivalent rules are provided under the non-Code provisions of ERISA.

Life insurance companies

The tax law provides special rules under which qualified pension, etc., plan assets (and related income, expense, gain, and loss) invested in annuity contracts issued by a life insurance company (or in the separate asset account of a life insurance company) are accorded similar tax treatment to that provided for assets held in a tax-exempt trust under a qualified plan (subchapter L).

General fiduciary standards; exclusive benefit of employees

The general fiduciary standards contained in the non-Code provisions of ERISA and the exclusive benefit rule of the Code regulate

[9] A shareholder-employee is an officer or employee who owns (or is considered to own under sec. 318(a)(1)) more than 5 percent of the stock of a subchapter S corporation.

the activities of fiduciaries and other persons involved in the administration of employee benefit plans. Under the non-Code standards of ERISA, each fiduciary[10] of an employee benefit plan must act solely in the interests of the plan's participants and beneficiaries, and must act exclusively to provide benefits to the participants and beneficiaries or to pay reasonable plan administrative costs. Under the non-Code standards, a fiduciary must exercise the care, skill, prudence, and diligence under the prevailing circumstances that a prudent man acting in a like capacity and familiar with such matters would use in conducting a similar enterprise. This "prudent man rule" applies (1) specifically to the investment of plan assets, and (2) to all other aspects of plan administration. The Act also prescribes the manner in which fiduciary responsibilities may be allocated and delegated among those persons involved in a plan's administration and the extent to which those responsibilities may be allocated and delegated.

Under the Code standards of ERISA, a qualified pension, etc., plan must be for the exclusive benefit of the employees or their beneficiaries. Accordingly, plan assets generally may not inure to the benefit of the employer before the plan's liabilities to employees and their beneficiaries are satisfied. To the extent that a fiduciary complies with the prudent man rule of the non-Code standards under ERISA, the fiduciary will be deemed to have complied with the prudent man aspects of the exclusive benefit rule of the tax standards of ERISA.

Under the non-Code standards of ERISA, the transfer or distribution of the assets of an employee welfare benefit plan upon termination of the plan is to be in accordance with the terms of the plan except as otherwise prescribed by regulations of the Secretary of Labor. Normally, the terms of the plan govern such a distribution or transfer of assets, except to the extent that implementation of the terms of the plan would unduly impair the accrued benefits of the plan participants or would not be in their best interests.

Also, under the non-Code standards of ERISA, on termination of a defined benefit pension plan to which the plan termination insurance provisions do not apply, the assets of the plan are to be allocated in accordance with the plan termination insurance provisions of ERISA governing allocation of assets except as otherwise provided in regulations prescribed by the Secretary of Labor.

The non-Code fiduciary responsibility standards of ERISA generally apply to all pension, etc., plans and welfare plans of employers or organizations in, or affecting, interstate commerce.[11] They do not apply to unfunded plans designed to provide deferral of compensation primarily for a select group of management or highly compensated employees, or to unfunded excess benefit plans.

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[10] For purposes of ERISA, a fiduciary with respect to a plan is a person who (1) exercises discretionary authority or control over management of the plan or any authority over management or disposition of its assets, (2) renders investment advice for a fee with respect to money or property of the plan or has authority or responsibility to do so, or (3) has discretionary authority or responsibility in the administration of the plan.

[11] There are exceptions for governmental plans, certain church plans, workmen's compensation plans, and nonresident alien plans.

Self-dealing standards

Self-dealing standards are provided both in the Code and non-Code provisions of ERISA. The Code provisions regulate self-dealing transactions involving "disqualified persons", while the nontax provisions regulate self-dealing transactions involving "parties-in-interest". These two terms have substantially similar definitions.

The self-dealing standards under the Internal Revenue Code apply to all pension, etc., plans which are (or have been) tax-qualified and to individual retirement accounts and annuities. The self-dealing standards under the non-Code provisions of ERISA apply to all plans to which the general non-Code fiduciary rules apply.

The self-dealing rules under both the Code and non-Code provisions of ERISA prohibit certain transactions between a plan and a disqualified person (or party-in-interest). Also, they prohibit use of plan assets or income for the benefit of a disqualified person (or party-in-interest).

Under the Code provisions of ERISA, a disqualified person who engages in prohibited self-dealing is subject to a two-level excise tax sanction. Initially, the disqualified person is subjected to a tax of 5 percent per year (or part thereof) of the amount involved in the act of self-dealing. A second tax of 100 percent of the amount involved is imposed if the act of self-dealing is not corrected by a specified date. These taxes are to be imposed automatically, that is, whether or not the self-dealer realizes that a violation has occurred and whether or not it can be shown that the particular violation harms the plan.

Under the non-Code provisions of ERISA, a fiduciary who knowingly engages (or should know that he engaged in) in prohibited self-dealing or otherwise breaches any of the responsibilities imposed by ERISA is personally liable to the plan for any losses it may suffer, and for any profits that the fiduciary may realize through the use of plan assets as a result of the misconduct. Also the fiduciary is subject to other appropriate sanctions as ordered by a court, including the fiduciary's removal. In addition, civil penalties (similar to the excise tax sanctions) may be imposed.

The Code and non-Code provisions of ERISA contain similar exceptions from the specifically enumerated self-dealing prohibitions. In addition to specifically enumerated exceptions to the prohibited self-dealing rules, ERISA provides for the granting of exemptions (variances).

Authority to promulgate regulations, rulings, opinions and exemptions under ERISA's fiduciary and self-dealing standards generally rests with the Secretary of Labor. The Treasury Department retains authority over those Code provisions governing employee stock ownership plans (ESOPs) and individual retirement accounts and annuities (IRAs). In addition, the Internal Revenue Service may disqualify a pension, etc., plan under the Code's exclusive benefit rule only after first consulting the Secretary of Labor.

Reporting and disclosure requirements

The Internal Revenue Code requires every employer who maintains a pension, etc., or other funded plan of deferred compensation (whether or not qualifed) to file an annual return stating such in-

formation as is required under Treasury regulations with respect to the plan's (1) qualification, (2) financial condition, and (3) operations. The Treasury may relieve an employer of the requirement of reporting information contained in other returns.

The non-Code rules of ERISA require the filing of an annual report with respect to most employee benefit plans (including welfare plans.) [12] A copy of the report must be available for inspection by participants and beneficiaries and, upon request, must be furnished to them. The non-Code provisions of ERISA list specific information generally required to be included in the annual report and give the Secretary of Labor limited authority to increase or to decrease the amount of information so required.

ERISA also requires the filing of a registration statement detailing the vested plan benefits of separated employees. The reports filed with the Internal Revenue Service and forwarded by the Service to the Social Security Administration so that retirees (or their beneficiaries) can be advised of private pension rights when application is made for social security benefits.

The non-Code provisions also require that each employee benefit plan file a summary plan description (and any material modifications or changes therein) with the labor Department. A summary annual report and a summary plan description (and any material modifications or changes therein) are required to be furnished to plan participants and beneficiaries.

The Labor Department, the Pension Benefit Guaranty Corporation, and the Internal Revenue Service follow a procedure under which a single report is filed only with the Service for each year of a plan. Under this procedure, the Service processes the reports and furnishes data to the Labor Department. The new procedure applies to pension, etc., plans and welfare plans.

Other standards

ERISA provides several other standards which are administered by the Treasury Department pursuant to Reorganization Plan No. 4. These standards apply with respect to—

(a) joint and survivor benefits,
(b) mergers and consolidations, of plans [13]
(c) assignment and alienation of plan benefits,
(d) the time that benefits commence,
(e) plan benefit reductions due to increases in social security benefits, and
(f) forfeiture of benefits upon withdrawal of employee contributions.

Civil and criminal sanctions

The Internal Revenue Code provides sanctions in the event that a pension, etc., plan is disqualified for failure to meet the standards

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[12] Under the non-Code rules of ERISA, an annual report is not required to be filed with respect to a governmental plan, a church plan which does not elect to be covered by the general provisions of ERISA, a workmen's compensation plan, a nonresident alien plan, or an unfunded excess benefit plan.

[13] The board of directors of the PBGC consists of the Secretaries of Labor (Chairman), Treasury, and Commerce.

prescribed for tax qualification (e.g., participation, antidiscrimination, and vesting). Penalty excise taxes are imposed on self-dealers and those who exceed the contribution limits for IRAs and H.R. 10 plans. Penalty excise taxes are also imposed on employers who fail to meet the minimum funding standards. In addition, penalties are imposed for failure to file reports on time.

On the Labor side, fiduciaries who violate standards may be forced to make up plan losses or disgorge profits and may be removed from office. Also, parties in interest may be subject to civil penalties. ERISA also provides criminal sanctions (up to a $5,000 fine and one year imprisonment for individuals and up to a $100,000 fine for others) for willful violations of the reporting and disclosure requirements.

ERISA also authorizes suits by participants or beneficiaries to enforce their rights under the plan or under the statute, or to enjoin violations of the plan or the statute. Suits also may be brought, under specified circumstances, by fiduciaries, the Labor Department, and the Treasury Department.

ERISA makes it unlawful to retaliate against anyone for exercising rights under an employee benefit plan or the Act, or for giving information in any inquiry or proceeding under the Act. Coercive interference with the exercise of any right under an employee benefit plan or the Act may be punished by a fine of up to $10,000 and imprisonment for up to one year.

Termination insurance

ERISA provides for insurance of vested employee benefits, up to specified limits, under defined benefit pension plans, under a program administered by the Pension Benefit Guaranty Corporation (PBGC).[13] Generally, only private, tax-qualified defined benefit pension plans are covered by the insurance.

To permit the PBGC to have advance notice of situations which may lead to plan termination, ERISA requires that certain events be reported to the PBGC within 30 days after their occurrence. Among these events are—

(a) notice by the Internal Revenue Service that a plan has ceased to qualify,

(b) a determination by the Internal Revenue Service that a plan has terminated or partially terminated, and

(c) failure of a plan to meet the minimum funding standard.

In addition, if the Internal Revenue Service finds a plan in which an event has occurred which it believes indicates the plan is unsound, the Service is required to notify the PBGC of the event.

In the event of the termination of an insured single-employer plan, plan assets are allocated to plan participants in accordance with a schedule contained in ERISA, and the PBGC insures a participant's benefits (up to the limits of the insurance) to the extent the assets allocated to the participant are insufficient. The PBGC provides financial assistance to distressed multiemployer plans.

[13] The board of directors of the PBGC consists of the Secretaries of Labor (Chairman), Treasury, and Commerce.

Tax treatment of pension, etc., plan distributions

Under the Code provisions of ERISA, the favorable income tax treatment of a lump sum distribution from a qualified pension, etc., plan is continued with modifications. In order to permit portability of benefits under a qualified pension, etc., plan, ERISA generally provides for the tax-free rollover of a lump sum distribution from one qualified plan to another (and between qualified plans and an individual retirement account, annuity, or bond). Under the Code, the tax-free rollover of an amount which does not qualify as a lump sum distribution also is permitted in some cases from a terminated qualified pension, etc., plan to another qualified pension, etc., plan or to an individual retirement account, annuity or bond. Under ERISA, as under prior law, a distribution from a qualified pension, etc., plan in a form other than a lump sum is generally taxed under the annuity rules.

The Code also provides estate tax and gift tax exclusions for amounts payable under qualified pension, etc., plans and individual retirement accounts, etc.

Explanation of Provisions

1. S. 2105

EBA established

The bill requires that the President establish, not later than two years after the bill's enactment, the Employee Benefit Administration (EBA) as an independent agency. The EBA is to be headed by a three-member board of directors consisting of an executive director and special liaison officers from the Treasury and Labor Departments. The three board members are to be appointed by the President, generally for six-year terms, subject to confirmation by the Senate. Not more than two board members could be affiliated with the same political party.

Under the bill, all policymaking and other functions of the Secretary of Labor under ERISA are transferred to the EBA. Generally all policymaking and other functions of the Secretary of the Treasury under ERISA and under those provisions of the Internal Revenue Code relating to qualified plans and employee welfare plans are also transferred to the new agency.

All officers and employees of the Department of Labor, the PBGC, and of the Department of the Treasury (including officers and employees of the Internal Revenue Service) who are primarily engaged in functions which are to be transferred to the EBA would be tranferred to the new agency. In addition, all officers and employees of the Joint Board for the Enrollment of Actuaries would be transferred to the EBA.

Transfers from the Treasury

Under the bill, overall responsibility for administering the tax laws (whether ERISA or pre-ERISA) relating to pension, profit-sharing, stock bonus, annuity, and bond purchase plans, would be transferred from the Treasury to the EBA. Thus, authority would be granted to the EBA to promulgate regulations, rulings, and opinions (and, where appropriate, to grant variances or waivers) under ERISA and the Internal Revenue Code with respect to, *inter*

alia, the following ERISA standards: (1) minimum age and service; (2) coverage; (3) vesting; (4) accrued benefits; and (5) funding. In addition, the EBA would be granted administrative authority for those Code provisions relating to the limitation on contributions and benefits under qualified plans, and those provisions providing special rules for qualified plans benefiting self-employed individuals or shareholder-employees of subchapter S corporations.

Under the bill, upon the request of the Secretary of the Treasury, the EBA would determine the tax qualification of any pension, etc., plan under ERISA's minimum standards and the Code's other tax-qualification rules. The new agency would then notify the Internal Revenue Service of its determination.

The bill would also transfer to the EBA administrative authority for the tax law relating to individual retirement accounts, annuities, and bonds (IRAs).

Under the bill, the EBA would also be granted authority to administer those provisions of the Internal Revenue Code relating to self-insured medical reimbursement plans maintained by employers, prepaid group legal services plans for employees, and deferred compensation plans of State and local governments. (The tax laws relating to these plans generally provide an income exclusion if certain requirements are met.) In addition, those Code provisions granting tax exemption to voluntary employees' beneficiary associations and to trusts providing supplemental unemployment compensation benefits would be administered by the EBA.

The bill would also transfer to the new agency administrative authority for the tax law relating to tax-sheltered annuity contracts purchased for employees by certain tax-exempt organizations and educational institutions.

Under the bill, if a penalty or excise tax is imposed under a provision of the Internal Revenue Code for which administrative authority is transferred to the EBA, the new agency would determine whether the penalty or tax is owed, and the amount of such penalty or tax, if any. The Secretary of the Treasury would be required to collect any penalty or excise tax certified by the EBA. However, the new agency generally could delay, reduce, or waive any penalty or excise tax imposed with respect to an employee benefit plan under the internal revenue laws.

The bill would also require the Treasury to make available to the EBA, at the agency's request, any return, document, or other item relating to any employee benefit plan or governmental plan.

Transfers from the Department of Labor

Under the bill, responsibility for administering those ERISA standards for which authority is presently assigned to the Secretary of Labor, including those relating to fiduciaries and acts of self-dealing, would be transferred from the Department of Labor to the EBA. In addition, the Department's responsibility to enforce ERISA standards by civil actions against plans and fiduciaries would be transferred to the new agency.

The bill would also transfer to the EBA responsibilities for administering the Welfare and Pension Plan Disclosure Act (WPPDA).

The bill directs that the functions of any other Federal agency be transferred to the EBA if the President determines that the transfer would further consolidate Federal administration of employee benefit plans.

2. S. 2106

S. 2106 does not provide for the establishment of the Employee Benefit Administration (EBA) as an independent Federal agency. Instead, under S. 2106 the Secretary of Labor would be responsible for administering the bill's provisions relating to public employee pension benefit plans. In addition, responsibility for administering and enforcing ERISA and those provisions of the Internal Revenue Code relating to employee benefit plans would remain, as under present law, with the Secretaries of Treasury and Labor.

Effective Dates

Under S. 2105, the transfers of administrative and enforcement responsibilities to the EBA would take effect upon the date the new Federal agency is established. Under a transitional rule, all actions taken by the Departments of Treasury and Labor, or any other agency or court, would continue in effect until superseded by action of the EBA.

The other provisions of the bills would be effective at the beginning of the second calendar year following the date of the submission of the report by the Advisory Council on Government Plans.

IV. BUDGET EFFECTS OF THE BILLS

The bills (S. 2105 and S. 2106) would have an undetermined effect on budget receipts and on budget outlays.

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