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S. Hrg. 103–443

RECENT COURT DECISIONS AFFECTING ERISA AND EXECUTIVE LIFE ANNUITIES

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Recent Decisions Affecting Erisa an...

HEARING

BEFORE THE

SUBCOMMITTEE ON LABOR

OF THE

COMMITTEE ON LABOR AND HUMAN RESOURCES UNITED STATES SENATE

ONE HUNDRED THIRD CONGRESS

FIRST SESSION

ON

S. 1312

TO PROVIDE FOR THE AVAILABILITY OF REMEDIES FOR CERTAIN FORMER PENSION PLAN PARTICIPANTS AND BENEFICIARIES, FOCUSING ON RECENT COURT DECISIONS THAT JEOPARDIZE WORKER AND RETIREE PENSION PROTECTIONS UNDER THE EMPLOYEE RETIREMENT INCOME SECURITY ACT (ERISA)

AUGUST 2, 1993

Printed for the use of the Committee on Labor and Human Resources

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RECENT COURT DECISIONS AFFECTING ERISA AND EXECUTIVE LIFE ANNUITIES

MONDAY, AUGUST 2, 1993

U.S. SENATE,
SUBCOMMITTEE ON LABOR, OF THE COMMITTEE ON LABOR AND HUMAN RESOURCES,
Washington, DC.

The subcommittee met, pursuant to notice, at 10:07 a.m., in room SD–430, Dirksen Senate Office Building, Senator Howard M. Metzenbaum (chairman of the subcommittee) presiding.

Present: Senators Metzenbaum, Wellstone, and Kassebaum.

OPENING STATEMENT OF SENATOR METZENBAUM

Senator METZENBAUM. Good morning, Senator Kassebaum, and witnesses.

Today the subcommittee will hear testimony from the Department of Labor and other interested parties on several recent court cases that jeopardize worker and retiree pension protections under the Employee Retirement Income Security Act, known as ERISA.

Two months ago, in a case called Mertens v. Hewitt Associates, the U.S. Supreme Court severely narrowed the protections available to workers and retirees under ERISA.

The Court held that ERISA did not clearly provide remedies to make aggrieved individuals whole and the Court, by a 5 to 4 majority, refused to read such remedies into ERISA. In addition, the Court cast doubt on whether ERISA provides a cause of action against individuals who knowingly participate in a violation of ERISA.

As a result of this case, the Department of Labor believes that its ability to enforce the law to protect pension plan participants is severely jeopardized. They are here today, and we will hear from them shortly.

In addition, the Department believes that its litigation against the Executive Life Insurance Company and the pension plans that bought shaky retirement annuities from Executive Life are at risk. As members of this committee well know, during the merger and takeover days of the 1980's, hundreds of companies terminated their pension plans and bought cheap, high-risk insurance annuities so that the company could pocket the funds remaining in the pension plan.

During the 1980's, over $20 billion was looted from workers' pension plans. In one of the most egregious cases, dozens of companies purchased insurance annuities from Executive Life which were

cheaper than other insurers, thereby directly benefiting the companies involved. Executive Life could offer higher rates of return because over 60 percent of its assets were speculatively invested in high-risk junk bonds.

As many experts predicted, the 1991, Executive Life filed for bankruptcy. As a result, 84,000 workers and retirees in 47 States had their retirement benefits reduced 30 percent for 1 year. Even though these retirees now are receiving their monthly retirement checks, they still do not have assurances that their benefits will be protected in the future.

The Secretary of Labor as well as private parties have dozens of lawsuits pending against the companies that bought these risky annuities. The Secretary of Labor believes that the Department's pending litigation in the Executive Life cases is in jeopardy as a result of the U.S. U.S. Supreme Court's decision.

This is not a new issue. For years, this committee has held hearings on the problems with ERISA enforcement. It is ridiculous to think that ERISA intended that individuals not be made whole if their benefits were wrongfully denied to them or misappropriated.

Last week, Senator Kassebaum and I introduced emergency legislation to protect all of the litigation pending in the Executive Life cases. These cases are close to the end of the statute of limitations and therefore could not be refiled if dismissed in the coming months. Senator Kassebaum and I are committed to passing this bill in the Senate in the coming weeks. There is no question in my mind that Congress intended to provide meaningful legal protection to the employee benefit promises made to millions of workers and retirees.

We cannot stand by and watch ERISA be dismantled by the courts. I plan to introduce comprehensive legislation in September to protect workers' pension benefit rights.

I look forward to hearing the testimony of today's witnesses and working with them to restore ERISA's promise to protect the pension and welfare benefit rights of working men and women.

I am very pleased that Senator Kassebaum, the cosponsor of this legislation, is here with us this morning. It is a privilege to have the opportunity to work with her.

Senator Kassebaum.

Opening Statement of Senator Kassebaum

Senator Kassebaum. Thank you, Senator Metzenbaum.

I would simply add that I am pleased that we could come up with this bill and that it would certainly be my hope we could expedite it and have it passed this week. If not, we do go into September, and that proves difficult.

During the time of the budget reconciliation bill's consideration on the floor, Senator Metzenbaum, Senator Kennedy and myself reached an agreement to take out provisions regarding civil penalties and liabilities which were far broader in scope and I felt had not been given the time and attention needed and went beyond, I could have argued, the bounds of the conference considerations on reconciliation.

But it is important to address the Executive Life situation, and I think that we are all sympathetic to the problems that have been

caused by that situation. I think S. 1312 really does that and provides a narrow enough focus that we can do so without questioning what the broader application may be which could have led to further legal action and further uncertainty. So it certainly is my hope that we can proceed ahead, largely because it is important that with the recent court decisions calling into question whether pension distribution annuities have standing to sue for relief under ERISA and whether, assuming a violation is found, a court can order relief for their lost benefits and help safeguard them against loss of benefits in the future.

I think that the legislation that we have introduced will do so and will allow for relief for pension distribution annuitants under the Executive Life case.

Thank you, Mr. Chairman.

Senator METZENBAUM. Thank you very much, Senator Kassebaum.

Senator Kassebaum, I hope you appreciate that this is a very auspicious occasion for us, because today is the first time that Olena Berg, at the Labor Department, will make an appearance before a committee of Congress.

We are delighted to have you with us this morning, and we look forward to your testimony.

STATEMENT OF OLENA BERG, ASSISTANT SECRETARY FOR PENSION AND WELFARE BENEFITS ADMINISTRATION, U.S. DEPARTMENT OF LABOR, WASHINGTON, DC, ACCOMPANIED BY ALAN D. LEBOWITZ, DEPUTY ASSISTANT SECRETARY, AND MARK MACHIZ, ASSOCIATE SOLICITOR OF LABOR FOR PLAN BENEFITS SECURITY

Ms. BERG. Thank you so much, Mr. Chairman.

Good morning, Mr. Chairman and members of the subcommittee. My name is Olena Berg. I am the assistant secretary of labor for pension and welfare benefits. With me are Alan Lebowitz, my deputy assistant secretary, and Mark Machiz, the associate solicitor of labor for plan benefits security.

I am pleased to be here to discuss the U.S. U.S. Supreme Court decision in Mertens v. Hewitt Associates, which weakened the security of pensions and health benefits for millions of workers.

We believe that congress enacted ERISA as a broad remedial statute. By a vote of 5 to 4, the U.S. U.S. Supreme Court in Mertens v. Hewitt Associates eliminate remedies and actions brought by participants and beneficiaries and by the Secretary of Labor, and we urge Congress to move quickly to reinstate those remedies.

Before describing our concerns, I want to thank the chairman and the members of the subcommittee for focusing attention on this issue. The Senate Labor and Human Resources Committee, under the bipartisan leadership of Senators Williams and Javits, was one of the authors of ERISA. We have appreciated your ongoing concern for vigorous enforcement of ERISA as evidenced by your concern that retirees get their benefits that were lost when Executive Life Insurance Company defaulted on its annuity obligations.

After Mertens, it is not clear that effective remedies are available in cases involving the improper choice of Executive Life or any

other insurance company as an annuity provider. In this regard, we compliment you, Mr. Chairman and Senator Kassebaum, for introducing legislation to address the annuity enforcement issue.

I want to be clear in telling you that Mertens threatens all of our enforcement efforts, not just the annuities cases. It ignores centuries of trust law that was embodied in ERISA. Instead of helping make workers' benefits more secure, ERISA under Mertens denies remedies for breach of trust that existed before ERISA was enacted.

My testimony today will discuss the need for corrective legislation to preserve essential relief so that justice can be rendered to participants and beneficiaries.

With respect to annuities, the Department has opened investigations in over 1,000 and conducted 85 onsite investigations. We have filed nine lawsuits in the annuities areas, directly affecting the benefits of over 16,000 participants. In many cases, as you pointed out, corporations willing to maximize the pension reversions terminated their plans and purchased the lowest price annuities rather than the safest available annuities, as is required by ERISA's standard of prudence. The risk of default is now borne by the retirees.

Even where a fiduciary admits to violating ERISA, courts may conclude under Mertens that they cannot reward retirees the difference between their promised benefit and the actual annuity payment. That is not even the worst case scenario. In the case of Kayes v. Pacific Lumber, a U.S. District Court held that the purchase of annuities from Executive Life deprived workers and retirees of the right to sue under ERISA for violations in the annuity purchase. That case says ERISA only allows participants and beneficiaries to sue for violations, and since the plan had been terminated, there were no longer any participants or beneficiaries.

These cases threaten lawsuits brought by the Department and by former plan participants and beneficiaries against fiduciaries who purchased annuities from Executive Life Insurance Company. This threat is based on ground of standing, or availability of relief, and certainly not on the merits.

While the California conservatorship and guaranty funds will limit the participants' losses and may in many cases make the participants whole, even in the best case, many participants will suffer substantial losses. Where a fiduciary violation in the purchase of annuity can be proven, the Department feels strongly that monetary relief should be available to make up the difference between the payments promised under the annuity and the payments actually made.

Instead, it may only be a matter of weeks before courts will be ruling on motions to dismiss the cases before them on the grounds that Mertens and Kayes do not allow relief for fiduciary breaches.

Again, we thank you, Mr. Chairman and Senator Kassebaum, for your prompt action to address this issue.

I would now like to speak more generally to the problems raised by the Mertens decision. First, it casts doubt on which remedies are available to address violations of ERISA. Second, the decision eliminates most liability on the part of nonfiduciaries who know-

ingly participate in fiduciary breaches. If the courts follow the dicta in Mertens, nonfiduciaries will not have any liability.

The Mertens case was a case against nonfiduciaries for knowingly participating in a fiduciary breach. However, the rationale of Mertens addressed available remedies and appears to deny most forms of monetary relief to individual participants and beneficiaries where fiduciary misconduct injures them personally rather than the plan as a whole.

While Mertens seems to allow a return of ill-gotten gains, in most cases, this is not sufficient to make good the entire losses. We do not believe Congress intended to deprive plan participants and beneficiaries of meaningful make-whole relief in such cases.

The Mertens case has drawn a lot of attention in part because it discussed, without deciding, the liability of third parties that knowingly participate in violations of ERISA. We are not talking about innocent service providers who are left holding the bag when something goes wrong. We are talking about male factors who should be held accountable when they actively and knowingly aid and abet fiduciaries in breaching their fiduciary duty and destroy the retirement security of the truly innocent.

Mertens held that a person who knowingly participates with a fiduciary in breaching ERISA is at most liable only to the extent he was unjustly enriched. To the extent the harm caused the plan exceeds the personal gain of the knowing participant, the plan is left without a remedy.

The majority opinion also contains dicta that questions whether any cause of action at all can be maintained against a knowing participant. A recent case litigated by the Department clearly illustrates the problem posed by the Court's dicta. In Reich v. Buckhannon, a suit was filed against the operators of a phoney health arrangement. The fiduciary defendants had bought "stop loss" insurance from the Madagascar American Bank and were paying approximately 70 percent of all employer contributions for this alleged insurance. This bank was not licensed by any State or Federal authority, was run out of a post office box, and its only assets consisted of worthless bonds from the Weimar Republic, the pre-Nazi Germany government.

In addition to the fiduciaries, who were judgment-proof, we sued the bank and its principal as knowing participants in the fiduciary's breach. The Mertens decision prevented us from seeking to make the plan whole by proceeding against the bank and its principal for losses to cover the plan.

As a result, benefit losses for claims totalling over $200,000 will fall on the shoulders of over 300 people who thought they were covered by the arrangement.

Another case brought by the Department of Labor has already actually been dismissed against the knowing participant based on the dicta in Mertens.

The amendments which we support to overturn Mertens would clarify that participants and beneficiaries who suffer a loss of benefit payments as a result of a fiduciary breach would have a meaningful remedy for such breach. Moreover, we believe that the amendments should also make clear that knowing participants in

a fiduciary breach are liable for damages under ERISA even if they are nonfiduciaries.

In addition, amendments are needed to assure that a former participant or beneficiary can bring an action for a violation that occurred while the plaintiff was a participant or beneficiary. Former participants or beneficiaries should also be able to obtain monetary relief in a suit by the Department.

Some have raised the specter that overturning Mertens would impose new liabilities and costs on plan sponsors and service providers. I do not think that there would be new liability costs. Until recently, nearly all the courts that considered whether there was liability for knowing participation in a fiduciary breach had held that there was such liability. In many circuits, the amendments that we seek have been the law for many years, and this has not resulted in the havoc now suggested by some critics.

Also, there was a split among the courts as to whether section 502(a)(3) afforded make-whole monetary relief to participants and beneficiaries. It is somewhat disingenuous for sponsors and service providers to claim that any amendments in this area would impose added costs and unexpected liabilities.

I want to stress that the administration favors the complete reversal of the Mertens decision so as to provide more comprehensive make-whole remedies for the Secretary of Labor and for participants and beneficiaries. We urge Congress to promptly enact amendments to ERISA along the lines which I have described.

Thank you for inviting me this morning. I would be pleased to answer any questions you may have.

[The prepared statement of Ms. Berg follows:]

Prepared Statement of Olena Berg

Good morning Mr. Chairman and members of the subcommittee. My name is Olena Berg. I am the Assistant Secretary of Labor for Pension and Welfare Benefits. Accompanying me are Alan D. Lebowitz, my Deputy Assistant Secretary, and Marc Machiz, the Associate Solicitor of Labor for Plan Benefits Security. I am pleased to appear before you to discuss our concerns regarding the recent U.S. Supreme Court decision in Mertens v. Hewitt Associates.

The U.S. Supreme Court in Mertens held that participants could not receive make whole relief under ERISA for benefits which they lost as a result of a fiduciary breach. We believe that this decision has made uncertain the protection of the benefits of millions of participants and retirees. We thank the Chairman and the Subcommittee for bringing attention to the need to reinstate the remedies eliminated by the U.S. Supreme Court, in a 5 to 4 decision. We believe that Congress in enacting the Employee Retirement Income Security Act (ERISA) intended to afford these remedies to participants, beneficiaries, and the Secretary of Labor.

The Senate Labor and Human Resources Committee has a long hand exemplary history of bipartisanship in protecting the interests of workers and retirees. It is well known that this Committee, under the bipartisan leadership of Senators Williams and Javits, was one of the authors of Title I of ERISA. More recently, this Subcommittee, its chairman, and its ranking members have been especially supportive of our efforts to protect the interests of plan participants, retirees and annuitants. We have appreciated your strong concern that ERISA be vigorously enforced, and that retirees receive the full value of their retirement promises in the face of the default by Executive Life Insurance Company on its annuity obligations. The Mertens case calls into question whether there will be any effective remedies available to Executive Life retirees or to the Secretary in cases involving loss of benefits as a result of the improper choice of Executive Life or any other insurance company as an annuity provider. In this regard we compliment you, Mr. Chairman, and Senator Kassebaum, for introducing legislation to address the annuity enforcement issue.

The Mertens decision, however, has implications for the structure of ERISA and its remedies that go far beyond our enforcement efforts in the annuities area. Indeed, it calls into question ERISA's grounding in the law of trusts, and the availability of remedies that existed for breach of trust and benefit denials long before ERISA was passed. The Department of Labor believes that Congress should at a minimum reinstate the remedies which the Solicitor General's brief in the Mertens case argued were available under section 502(a) (3), and which was the position of the four dissenting Justices. My testimony today will discuss several problems of broad scope that were raised by the Mertens decision, and which must be addressed to preserve the relief that is essential for justice to be rendered to participants and beneficiaries who are illegally denied benefit payments. However, I believe it is important that we initially understand the significant impact the decision will have on pending litigation if the amendments we support are not adopted.

IMPACT ON PENDING LITIGATION

The Department of Labor has undertaken a major annuity enforcement effort. This effort is the byproduct of the junk bond and leveraged buyout fever of the 1980's. The greed of the times was typified by the desire of heavily leveraged corporations to maximize pension reversions by using the assets their terminated plans to purchase less than the safest available annuities for their plan participants.

The activities of this Subcommittee, led by the Chairman and Senator Kassebaum, who were concerned that the purchase of annuities from Executive Life would be an ERISA violation, and our investigative efforts stopped the Coleman company from purchasing millions of dollars in questionable annuities. The Department of Labor investigated Coleman's arrangement to purchase annuity contracts from Executive Life to satisfy its pension liabilities and the deal was canceled before annuity contracts were issued to participants and beneficiaries of the pension plan. While we had some investigations already underway, the concern of this Subcommittee over threats to retirees led former Secretary Elizabeth Dole to direct the initiation of a major enforcement effort in the annuities area several years ago.

Over the past several years, the Department opened investigations in over a thousand cases and conducted on-site investigations in 85 cases. Our investigations have involved many major corporations, including Coleman, Pacific Lumber, Maxxam Industries, National Can, Raymark, Revlon and others.

In many of the cases we investigated, annuities were purchased from annuity providers that had offered the lowest price but that were not, by objective criteria, the safest available annuity provider. This amounts to a violation of the fiduciary obligations of ERISA. The Mertens decision may, however, result in courts ruling that they cannot make a participant whole for any diminution in the value of benefits that results from the violation. This is because Mertens appears to deny most forms of monetary relief where the remedies run to the individual participants and beneficiaries rather than to the plan. Even where a breach of fiduciary duty results in the participant receiving an annuity that no longer pays the full amount of the pension benefit, a court may conclude that it is not able to order the breaching fiduciary to pay the retiree the difference between the promised benefit and the actual annuity payments.

Furthermore, in the case of Haves v. Pacific Lumber, the U.S. District Court for the Northern District of California held that former participants and beneficiaries who were given Executive Life annuities do not have standing to sue under title I of ERISA, even though they were only seeking to remedy a violation of ERISA that occurred while they were still participants and beneficiaries.

The court decisions in Mertens and Haves threaten a number of lawsuits brought by the Secretary of Labor and by former plan participants and beneficiaries against plan fiduciaries who purchased annuities from Executive Life Insurance of California without complying with ERISA's fiduciary duties of prudence and loyalty. This threat is based on grounds of standing or availability of relief, rather than on the merits. The proposed amendments to ERISA that were adopted by the Senate Labor and Human Resources Committee in budget reconciliation would have clarified that such relief is available under ERISA. In the case of a fiduciary violation in the purchase of an annuity contract, this would include monetary relief to make up the difference between the payments promised under the annuity and payments actually made.

Our concerns with availability of relief and the nature of relief available are not abstract concerns. The Department of Labor has filed nine lawsuits in the annuities area, directly affecting the benefits of over sixteen thousand participants.The total dollar value of questionable annuities in our Executive Life investigations is about

one billion dollars. To cite just one example, our pending lawsuit against Pacific Lumber involves an Executive Life annuity which cost $37.2 million and which could-result in lost benefits to approximately three thousand participants.

We of course recognize that the California conservatorship and State guarantee funds will limit the participants' losses and may in many cases make the participants whole. However, even in a best case scenario, many participants will suffer substantial losses out of the conservatorship.

I have attached a list of annuities lawsuits which the department has brought or participated in. In addition, participants and beneficiaries have brought a number of private lawsuits in this area. It may be only a matter of weeks before courts will be ruling on motions to dismiss the cases before them, on the grounds that under Mertens and Kayes, even if there is a fiduciary breach, there is no standing to seek relief or no remedy available, or both. In the absence of legislative amendments, our efforts in the annuities area could be wasted.

OTHER ISSUES RAISED BY MERTENS

I would now like to address the specific problems raised by the Mertens decision. Our concerns fall into two categories. First, the decision casts doubt on which remedies are available to redress violations of ERISA. Second, the decision eliminates most liability on the part of nonfiduciaries who knowingly participate in fiduciary breaches. Moreover, if the courts follow the dicta in Mertens, nonfiduciaries will not have any liability under ERISA. I will address each of our concerns in turn.

1. REMEDIES UNDER ERISA

The Mertens case involved a suit against nonfiduciaries for knowingly participating in a fiduciary breach. The rationale of the Mertens decision, however, appears to deny most forms of monetary relief to individual participants and beneficiaries where fiduciary misconduct injures them personally, rather than injures the plan as a whole. For example, under the Internal Revenue Code, a pension plan must provide notice to participants who are leaving the plan of their right to have lump-sum distributions rolled over into another plan or an IRA. If such a rollover is not timely made, the benefits will be immediately subject to taxes. A fiduciary's failure to follow plan provisions regarding the giving of such notice is a breach of fiduciary duty under ERISA, even though the fiduciary is not enriched by the breach. Thus, under Mertens there is no remedy to the participant who suffers adverse tax consequences because of such a breach. This was the result in Novak v. Andersen Corn., a-case decided by the Eighth Circuit Court of Appeals. A few days after its decision in Mertens, the U.S. Supreme Court predictably denied a petition for writ of certiorari filed by the participant in Novak.

In most cases, a return of ill-gotten gains is not sufficient to make good the losses of participants and beneficiaries. Where the fiduciary cannot be made to restore assets lost as a result of a breach to the plan because the plan has terminated, a court may rule that there is no remedy available to the Secretary or the former participants and beneficiaries to redress the breach. We do not believe Congress intended to deprive plan participants and beneficiaries of meaningful remedies in such cases.

2. LIABILITY FOR KNOWING PARTICIPATION IN FIDUCIARY BREACHES

The Mertens case has drawn a lot of attention in part because it discussed, without deciding, the liability of third parties that knowingly participate in violations of ERISA. It is important to remember that we are not talking about innocent third parties who are left holding the bag when something goes wrong. We are talking about wrongdoers who should be held accountable when they actively and knowingly aid fiduciaries in breaching their fiduciary duty, breaches that may destroy the retirement security of truly innocent people, namely the participants and beneficiaries of the plans. The five Justice majority in Mertens indicated that, if the issue were squarely before them, they might well find that there is no such liability under ERISA. In fact, in an action brought by the Department to protect participants from a breach of fiduciary duty by a plan trustee with the knowing participation by an insurance company, a District Court dismissed the case against the knowing participant on the grounds that, under Mertens, there is no remedy available against a nonfiduciary who knowingly participated in the fiduciary breach.

Mertens held that if there is a cause of action for knowing participation in a fiduciary breach a nonfiduciary who knowingly participates with a fiduciary in breaching ERISA, is, at most, monetarily liable only to the extent he was unjustly enriched.Thus, the plan is left without a remedy against the knowing participant to the extent the harm caused the plan exceeds the personal gain of the knowing par-

ticipant. A case decided prior to Mertens illustrates how a nonfiduciary can be a key component to carrying out a fiduciary violation, and that such nonfiduciaries do not always receive the benefit of the violation. In a 1989 case brought by the Department in Texas, Dole v. Lundberg, a plan fiduciary who was also an officer of the plan sponsor devised a scheme for hiding the use of plan assets by himself and the sponsoring company. The fiduciary enlisted a nonfiduciary who was willing to accept $2.5 million in loans from the plan and then immediately reloan the proceeds to the fiduciary and plan sponsor. For this service, the nonfiduciary was paid approximately $50,000 as a fee, yet the use of this "straw man" made the breach of trust much more difficult to detect. Although the nonfiduciary's knowing participation in the breach was clear, under the rationale of the Mertens decision it would appear that he would be liable, if at all, only for the return of his fee.

In addition to the holding in Mertens that seriously curtails the remedies available against a nonfiduciary, the majority opinion contains dicta that questions whether any cause of action at all can be maintained against a knowing participant. Two recent cases litigated by the Department clearly illustrate the problem posed by the Court's dicta. In the first case, Reich v. Buckhannon, a suit was filed against the operators of a phoney health arrangement which was masquerading as a welfare plan. The fiduciary defendants had bought "stop loss" insurance from something called the Madagascar American Bank and were paying approximately 70 percent of all employer contributions for this alleged "insurance." This "bank" was not licensed by any State or Federal authority, was run out of a post office box and its only assets consisted of worthless bonds issued by the Weimar Republic, the pre-Nazi government of Germany. In addition to the fiduciaries, who are judgment proof, we sued the bank and its principal as knowing participants in the fiduciaries' breach. In this case, had the court followed the Mertens dicta we would not have been successful in obtaining a court order recovering for the plan all of the money which had been paid to the bank. The Mertens decision, however, did prevent us from seeking to make the plan whole by proceeding against the bank and its principal for losses caused to the plan. As a result, benefit losses for claims totalling over $200,000 will fall on the shoulders of over three hundred people who thought they were covered by the arrangement.

In the second case, we were even less fortunate. In Reich v. Continental Casualty Company, we sued the trustees of a plan who had spent about one million dollars of plan assets to buy one million dollars of fiduciary liability insurance. Prior to the purchase, we had sued the same trustees regarding another matter after which the insurance company canceled its policy. Facing a second lawsuit by the Department, the trustees, we alleged, simply transferred their fiduciary exposure to the plan by buying one million dollars of such coverage for themselves with nearly one million dollars of plan assets instead of exercising a rider which would have allowed them to retain five million dollars of coverage for their past conduct. Thus, when we filed the second suit, our recovery, paid by the insurance company, provided virtually no net restitution to the plan because of the excessive premium the trustees had paid. The insurance company, rather than facing five million dollars of exposure, had reduced its exposure to zero. This insurance transaction led to our suing the trustees a third time and, this time, we also sued the insurance company as a knowing participant to recover the excessive premium paid by the trustees out of plan assets. Despite contrary precedent in its own circuit and despite its recognition that the U.S. Supreme Court's discussion of knowing participation in Mertens was dicta, the Court dismissed our knowing participation claim against the insurance company. The Court stated that, "[I]t would be foolish—to ignore the U.S. Supreme Court's relatively extended and careful statement of its views on the subject—merely because it is dicta."

Prior to Mertens, five of the Circuit Courts of Appeals which considered the issue found that knowing participants in a fiduciary breach are jointly and severally liable under ERISA for losses resulting from the breach. Only two Circuit Courts of Appeals held otherwise. The principle of liability for knowing participation in a fiduciary breach accords with the long established rule under the common law of trusts. We urge Congress to enact amendments that would make clear that some of the remedies that were available before ERISA for knowing participation in a fiduciary breach are still available.

Some have raised the specter that amendments to overturn Mertens would impose new liabilities and new costs on plan sponsors and their service providers. I do not think that there would-be new liability costs. Until recently, nearly all the courts that considered whether there was liability for knowing participation in a fiduciary breach had held that there was liability. In many circuits, the amendments we seek have been the law for many years and this has not resulted in the havoc now suggested by some critics. Also, there was a split among the courts as to whether sec-

tion 502(a) (3) afforded make whole monetary relief to participants and beneficiaries. So, it seems to me somewhat disingenuous for sponsors and service providers to claim that any amendments in this area would impose added costs and unexpected liabilities.

Concerns have also been raised that the legislation in this area would impose liability on a doctor who participates in a decision not to provide a certain treatment under a managed care program. This is not the case. Good faith medical advice that results in a benefit denial does not constitute knowing participation in a fiduciary breach under ERISA, even if a court ultimately determines that the plan provides for such benefits.

CONCLUSION

It is important to realize what the amendments we support in this area would and would not do. The amendments which we support to overturn Mertens would clarify that participants and beneficiaries who suffer a loss of benefit payments as a result of a fiduciary breach would have a meaningful remedy for such a breach. Such amendments would be particularly appropriate in the Executive Life situation. Moreover, the amendments we support would also make clear that knowing participants in a fiduciary breach are liable for damages under ERISA, even if they are nonfiduciaries. I know of no principle of equity that says that a person who participates in a harm to another person should be able to thumb his nose at the victim. But that may well be the result if the U.S. Supreme Court rules that there is no remedy under ERISA against a knowing participant in a fiduciary breach, and courts then rule that lawsuits in State courts against a knowing participant are preempted by ERISA. While we believe that claims against professionals, such as attorneys, accountants, and actuaries, who commit malpractice against a plan are not protected by ERISA's preemption provisions from State remedies,such remedies will not likely be pursued by breaching fiduciaries who have been assisted in their misconduct and cannot be pursued by the Department of Labor. Furthermore, there may be no effective remedies against knowing participants in a fiduciary breach who are not professionals.

In addition, amendments are needed to assure that a former participant or beneficiary has standing to bring an action based on a violation that occurred when the plaintiff was a participant or beneficiary. This would deal with the problem raised by the Kayes decision. Such former participants or beneficiaries should also be able to obtain monetary relief in a suit brought by the Secretary of Labor.

We would propose to make these amendments applicable to any case that is brought on or after the date of enactment and to any case that is pending, including pending on appeal, on or after enactment.

In conclusion, I want to stress that the Administration favors a complete reversal of the Mertens decision so as to provide more comprehensive remedies for the Secretary of Labor and for participants and beneficiaries. We urge Congress to promptly enact amendments to ERISA along the lines which I have described.

CASES INVOLVING EXECUTIVE LIFE INSURANCE PENSION ANNUITIES

When Executive Life Insurance of California was taken over by the State insurance regulators in April 1991, it had issued pension distribution annuities covering over 44,000 retirees. The annuitants in pay status suffered an immediate 30 percent cut in the amount of their payments. This situation continued until May 1992, when full payment was provisionally restored for most annuities with a present value of less than $100,000 pursuant to a "quick pay plan" worked out by State insurance guaranty associations. The quick pay plan does not apply to annuitants residing in the District of Columbia, Colorado and Louisiana because these jurisdictions did not have guaranty associations when Executive Life was placed in conservatorship.

The Department of Labor investigated 43 pension plans that had purchased Executive Life annuities and has to date brought 8 lawsuits.

Martin v. Maanetek (E.D. Wis.) principal location of employer: Wisconsin cost of annuity: $23.4 million. Number of participants: 1,900.

Status: Settled.

Reich v. Pacific Lumber Co., (N.D. Cal.) principal location of employer: California. Cost of annuity: $37.2 million. Number of annuitants: 3,000. Status: Pending.

Reich v. AFG Industries (N.D. Tex.) principal location of employer: Pennsylvania. Cost of annuity: $12.4 million. Number of participants: 1,300. Status: Pending.

Reich v. Geosource (S.D. Tex.) principal location of employer: Texas. Cost of annuity: $26.6 million. Number of participants: 2,950. Status: Settled.

Reich v. Smith International (C.D. Cal.) principal location of employer: California. Cost of annuity: $51 million. Number of participants: 3,100. Status: Pending.

Reich v. BMC Industries (E.D. Minn.) principal location of employer: Minnesota. Cost of annuity: $2.5 million. Number of participants: 94. Status: Pending.

Reich v. Raymark Industries (D.Conn.) principal location of employer Connecticut. Cost of annuity: $49.4 million. Number of participants: 2,300. Status: Pending.

Reich v. American National Can Co. (N.D. Ill.) principal location of employer: Illinois. Cost of annuity: $ 21.4 million. Number of participants: 750. Status: Pending.

In addition, a number of private suits have been filed. The following is a list of those that have come to the Department's attention.

Miller v. Pacific Lumber (N.D. Cal.) covers same plan as Reich v. Pacific Lumber. Status: Dismissed for lack off standing; motion for reconsideration pending.

Waller v. Blue Cross of California (9th Cir.) principal location of employer: California. Cost of annuity: ? Number of participants: ? Status: Summary judgment granted for defendants in district court; appeal pending (DOL has filed an amicus brief).

Gumbinger v. Revlon. Inc. (S.D.N.Y.) principal location of employer: New York. Cost of annuity: ? Number of participants: More than 1,000. Status: Pending.

Doualas v. Viehman (W.D. Pa.) principal location of employer (H.H. Robertson): Pennsylvania. Cost of annuity: $18.6 million. Number of participants: ? Status: Pending.

Dodson v. Lone Star Technologies. Inc. (S.D. Tex.) principal location of employer: Texas. Cost of annuity: $30 million. Number of participants: 500. Status: Pending.

Calabrace v. American National Can Co. (N.D. Ill.) covers same plan as Reich v. American National Can Co. Status: Pending.

In re Budd Co. Pension Plan Litigation (E.D. Pa.) principal location of employer: Pennsylvania. Cost of annuity: $7 million. Number of participants: 1,000. Status: Pending (DOL has filed an amicus brief in opposition to defendants motion for summary judgment).

Bussian v. RJR Nabisco, Inc. (S.D. Tex.) principal location of employer: Texas. Cost of annuity: $55 million. Number of participants: 1,500. Status: Pending.

In addition, the Department of Labor has brought one lawsuit against the fiduciaries of a plan that purchased an annuity from presidential Life Insurance Co., which has not been taken over by State authorities. Insurance rating services, however, have lowered their ratings of the company. No reduction in annuity payments has yet occurred.

Reich v. Strouse Adler. Inc. (D. Conn.) principal location of employer: Connecticut. Cost of annuity: $1.3 million. Number of participants: 117. Status: Pending.

Senator METZENBAUM. Thank you very much, Ms. Berg.

Senator Wellstone, did you wish to say a word?

OPENING STATEMENT OF SENATOR WELLSTONE

Senator WELLSTONE. Thank you, Mr. Chairman.

I just want to apologize to Ms. Berg. I have to manage the Tom Payzant nomination at 10:30, so I have to leave. But I came by to show my very strong interest. I just think what we are looking at is extremely important, and both to you, Mr. Chairman and Senator Kassebaum, our office will take a very, very close look at this legislation which you have introduced. And understanding full well, Mr. Chairman, that you and I usually are in agreement, I'll just bet we will be strongly behind you.

And I apologize for having to leave. I just didn't want you to think that my coming and leaving was for lack of interest; is it just because of this conflict in schedule.

Thank you.

Ms. BERG. Thank you.

Senator METZENBAUM. The good news, Senator Wellstone, is that not only are you and I in agreement, but more importantly, Senator Kassebaum and we are in agreement.

Senator WELLSTONE. I try to scrupulously avoid this question of the extent to which Senator Kassebaum and I are in agreement, but it seems like it's happening more and more.

Thank you, Mr. Chairman.

Senator METZENBAUM. Thank you very much, Senator Wellstone, for being with us.

We will now receive a statement for the record by Senator Dodd.

[The prepared statement of Senator Dodd follows:]

PREPARED STATEMENT OF SENATOR DODD

Mr. Chairman, this morning's hearing considers legislation critical to thousands of workers across the United States—including several thousand in my State.

In the 1980's, many companies, large and small, terminated their pension plans and bought insurance annuities to provide the retirees with their pension benefits. Unfortunately, some companies, in effect, chose "the lowest bidder" and purchased annuities that were based on speculative investments and junk bonds.

Such was the case with executive life annuities. When the performance of these investments fell, so did the executive life insurance company—leaving 84,000 pensioners without promise of their full retirement benefits.

Many of the companies who relied on Executive Life to provide for their retirees have stepped forward to make up the full benefits as originally promised. But other retirees continue to receive fewer benefits and have no sure promise of full and continuing benefits in the future.

The Department of Labor and these retirees have rightly gone to court to obtain their pension benefits as promised, suing under the Employee Retirement Income Security Act (ERISA). Two thousand pensioners in Connecticut are currently involved in such a case, Reich v. Raymark Industries.

Earlier this summer, the U.S. Supreme Court, in Mertens v. Hewitt, reached a decision that seems to have narrowed the legal protections available to these retirees. While some may continue to argue that this case did not have this effect, in my mind, it is clear that the Court's arguments could be read that way. And I am not willing to take that risk with the security of tens of thousands of retirees hanging in the balance.

The legislation we have before us today, sponsored by Senator Metzenbaum and Senator Kassebaum, is clearly narrowly written to address this specific situation and to assure these pensioners of their rights under ERISA.

I greatly appreciate the leadership of Senator Metzenbaum, who has so long been the conscience of the Senate on these issues, and Senator Kassebaum, whose constructive efforts in this matter have been most helpful. I look forward to today's hearings and to working with you, Mr. Chairman, and Senator Kassebaum to move this important legislation. Thank you.

Senator METZENBAUM. Ms. Berg, am I correct in understanding that the Labor Department has consistently taken the position both in Democrat and Republican administrations that monetary remedies exist for violations of ERISA?

Ms. BERG. Yes, we have, Mr. Chairman.

Senator METZENBAUM. What type of remedies were available to individuals prior to enactment of ERISA, if you know?

Ms. BERG. Prior to the enactment of ERISA under trust law, we believe make-whole monetary relief was available in this type of

case. In fact, the minority, four members of the U.S. U.S. Supreme Court, pointed that out in their write-up of the decision.

Senator METZENBAUM. Is it true that workers and retirees currently have less legal protection than they enjoyed prior to ERISA, by reason of the Mertens decision?

Ms. BERG. We definitely belief so.

Senator METZENBAUM. And isn't it true that under the Mertens decision, there is no monetary remedy, even if a breach of the law results in workers receiving a smaller benefit than the benefit to which they were entitled?

Ms. BERG. That's right.

Senator METZENBAUM. To what extent does the Department believe that its ability to protect workers and retirees has been impaired by the courts?

Ms. BERG. We believe it has been greatly impaired, both on the issues of remedies, which you have just mentioned, and on the issue of going after knowing participants.

Senator METZENBAUM. You talk about the fact that there may not be a cause of action against nonfiduciaries under ERISA. What types of other individuals are you talking about?

Ms. BERG. As in the example I gave, in that case, it was the bank that accepted the 70 percent of employer contributions and provide no insurance, leaving members of the plan totally unprotected. We have another example that I'd like to hope wasn't typical, but may well be, of a fiduciary who essentially laundered money through someone else by providing a quote-unquote "loan" for $2.5 million to a nonfiduciary, who then simply returned the money back to the fiduciary and plan sponsor to use for illegal purposes. That made it very difficult for us to discover the misuse of the funds, and the person involved, the nonfiduciary involved, was paid $50,000 for participating in the money laundering.

Now, under Mertens, at best, all we could do we get the person to give the $50,000 back, and if you abide by the dicta in Mertens, we'd have no remedy at all against that person, and clearly the breach could not have taken place without that active participation.

Senator METZENBAUM. What is the legal standard for determining when a nonfiduciary has knowingly participated in a violation of the law, and is this a tough standard, or could it include passive activity, as has been claimed?

Ms. BERG. The standard is to "knowing induce, aid, abet, or undertake to conceal." I think that is a pretty high standard and clearly would not include passive activity.

Senator METZENBAUM. I have no further questions.

Senator Kassebaum.

Senator KASSEBAUM. Thank you, Mr. Chairman.

Ms. Berg, let me just ask a little bit about this bill under consideration and how you view that.

Do you agree with our understanding that this bill before us does not change the obligation to the fiduciaries under ERISA?

Ms. BERG. The bill that you are presenting before us, as we understand it, would address the remedies and standing issues in the annuities cases and does not address the knowing participation issue.

Senator KASSEBAUM. On the knowing participation issue, I found it interesting in the case you mentioned about the Madagascar bank, a clearly fraudulent operation. Was there not some way of monitoring that? At what point is there some protection early on in following the placement of annuities?

Ms. BERG. Well, a lot of these cases are going to be difficult to uncover before there is evidence, like the nonpayment of claim, that indicates that something is wrong. I would argue that that is why it is so important that we have some form of action against a nonfiduciary who participates in this because you need a deterrent effect. And if a participating nonfiduciary realizes that the worst thing that is going to happen to them is that they have to return their fee for having participated, or worse yet, under Mertens, nothing can happen to them, there is no deterrent effect whatsoever.

So again, I would argue that the responsibility, knowing that you were going to have to make whole monetarily the people that you injured, is the best remedy that we could have.

Senator KASSEBAUM. What has happened to that Madagascar bank now? Does anybody know? I wonder if there is a bankruptcy there. Again, we are faced with these situations where, in the case of Executive Life, one could have hoped the handwriting was on the wall, and there would have been some steps earlier on. I guess I am arguing on beyond this situation, just trying to figure out how we can be sure we can define it in such a way that we don't paint it with such a broad brush, and we catch those who are doing their job and adhering to their responsibilities and those who are not. And again, it goes to passive or active participants in many ways.

Yes, it sounded like a high standard that you mentioned, but I think this is something that we do need to carefully think through, and again, assume greater responsibility earlier on than we have, I think, in the past.

Would you agree that in order to sue under this bill, a plaintiff must establish a violation of a fiduciary provision?

Ms. BERG. Yes.

Senator KASSEBAUM. Under this bill, what damages do you believe could be awarded?

Ms. BERG. I think the bill is clear that the damages are the difference between the annuity that they are receiving and the benefit they would have received had the violation not occurred.

Senator KASSEBAUM. And in your consideration of looking at overturning the Mertens decision, this is something that you feel strongly should be concentrated on, though, as far as damages and going on beyond just those——

Ms. BERG. I'm sorry. I want to be sure that I understood the question.

Senator KASSEBAUM. Expanding damages, you believe should be considered.

Ms. BERG. Our position is that we would like to see the law returned to what we believed it was right before the Mertens decision, that is, participants and beneficiaries can get make-whole monetary relief, just as your bill does; they could receive the benefits to which they were entitled had the breach not occurred. We

are not looking for an expansion of damages into areas that the courts had not awarded them pre-Mertens.

Senator KASSEBAUM. If the Department of Labor seeks changes in damages under ERISA—but you say you really aren't, that you would only hope to see it maintained as it was pre Mertens decision——

Ms. BERG. Exactly.

Senator KASSEBAUM. [continuing]. But if there would be a desire to expand damages, might not this be something that should be considered in the light of welfare reform and health care reform and some of the big initiatives that are going to be out there.

Ms. BERG. Certainly any expansion of damages should be very carefully considered as part of an overall action like that.

Senator KASSEBAUM. Thank you very much.

Senator METZENBAUM. Thank you very much, Senator Kassebaum.

Thank you very much, Ms. Berg. We look forward to continuing to work with you over a period of time.

Thank you.

Ms. BERG. Thank you.

Senator METZENBAUM. Our next panel includes Mr. Jack Miller, of Denton, TX; Mr. Al Sigman of Sigman & Lewis of San Francisco; Ms. Vicki Gottlich, staff attorney with the National Senior Citizens Law Center of Washington, DC; Mr. John Vine, partner in Covington & Burling, on behalf of the ERISA Industry Committee, Washington, and Mr. James Klein, executive director of the Association of Private Pension and Welfare Plans of Washington, DC.

I think all of you know the committee has a 5-minute rule. It is my understanding that Mr. Sigman and Mr. Miller are going to testify jointly is that correct?

Mr. SIGMAN. I am representing Mr. Miller in the litigation. I am here to advise him as may be necessary during the course of these proceedings. But the statement is Mr. Miller's.

Senator METZENBAUM. We are happy to have you with us, Mr. Sigman.

Mr. Miller, please proceed.

STATEMENTS OF JACK MILLER, DENTON, TX, ACCOMPANIED BY AL SIGMAN, SIGMAN & LEWIS, SAN FRANCISCO, CA; VICKI GOTTLICH, STAFF ATTORNEY, NATIONAL SENIOR CITIZENS LAW CENTER, WASHINGTON, DC; JOHN VINE, PARTNER, COVINGTON & BURLING, ON BEHALF OF ERISA INDUSTRY COMMITTEE, WASHINGTON, DC, AND JAMES KLEIN, EXECUTIVE DIRECTOR, ASSOCIATION OF PRIVATE PENSION AND WELFARE PLANS, WASHINGTON, DC, ACCOMPANIED BY TED RHODES, GENERAL COUNSEL

Mr. MILLER. Thank you, Senator. I appreciate the opportunity of being here today.

Listening to your introductory remarks, it seems like deja vu all over again, and also to Secretary Berg, and I'll refer to her comments in just a moment.

I retired from Victor Equipment Company in Denton, TX in 1988, where I served for over 14 years as vice president of personnel. Victor was a wholly-owned subsidiary of Pacific Lumber Company.

Secretary Berg alluded to a recent court case that was thrown out of court. I am a named plaintiff in that case. Despite my status as a plan participant from my former employer, a Federal judge on May 17th ruled that I and seven other plaintiffs in a lawsuit against Pacific Lumber Company lacked standing under ERISA to sue for breach of ERISA fiduciary duty. The judge ruled that we are only former participants of a terminated plan and therefore lack standing—even though our lawsuit alleged flagrant violations of fiduciary duty in the way the plan was terminated.

The judge's ruling in throwing our case out of court created what I consider the proverbial "Catch-22" situation. The plan was terminated, and it generated a burden on myself and many of my fellow employees; and yet, even though illegal acts may have been committed in the process of this, we are now told we have no legal rights, no rights of redress under the law.

The judge's reasoning left participants and beneficiaries stranded, a ruling that plan beneficiaries could avoid any liability for breaches of fiduciary duty in essence by simply terminating a plan. Once the plan is terminated, participants and beneficiaries could do nothing about the breaches, no matter how blatant, willful, harmful to participants and beneficiaries.

Thus, our access to the courts at this time seems to be blocked despite what we feel is the intent of Congress and the intent of ERISA.

Let me now give a little personal background on myself and some of the former employees that I worked with and how this impacted us.

I live in Denton, where I worked. I live there with my wife of over 40 years. She is a probation officer in the Denton County court system. After 14 years with Victor, I retired, and I currently do human resource consulting work on a part-time basis, and I spend much of my time as a city council member in Denton, a personally rewarding but not financially rewarding position. And in my spare time—you have heard of the proverbial "Mr. Mom"—well, in my spare time, I act as "Mr. Grandmom" to a 10-year-old grand-daughter. We have four children ages 28 to 39, and one of those children and our grand-daughter live with us, and I have the honor of being "Mr. Grandmom" to my grand-daughter.

Incidentally, as I was getting ready to come to Washington last week, I got some advice from some of my family and my associates. My wife said, "Don't forget to pat your hair," because it tends to blow in the wind, "and don't talk too fast." My grand-daughter said, "Don't forget to bring me something from Washington." My fellow council members said, "Don't embarrass us." And some of my constituents said, "Don't come back." But I intend to do it, anyway.

I became involved in the litigation that was referred to in 1991. The collapse of the Executive Life Insurance Company and the resultant 30 percent reduction of my monthly pension benefits and those of my fellow plan members from that company really jolted me and really jolted us. I'll have more about this to say in a minute.

Because of my former human resources position at Victor, I got to know most of our people very well. We have great people down there who worked for and continue to work for Victor and were in

the retirement plan. I communicate regularly with them, both current employees and retired employees, periodically giving them information on the Pacific Lumber and Executive Life scenario.

Our people down there are a closeknit group, and when we get information like this, it spreads like wildfire through the community.

Going back, sometime in late 1985 or early 1986, the Pacific Lumber Company, which owned Victor at that time, was taken over in a highly-leveraged buyout. At that time, Pacific Lumber owned manufacturing divisions and operations in San Diego and Los Angeles, CA; Denton, TX; Wichita, KS; Huntsville, AL; Danvers, MA, and East Lebanon, NH. The units manufactured cutting and welding products and were known as the cutting and welding subsidiaries. Hundreds of employees of these units were plan participants of the Pacific Lumber Company plan as were the people who were in the logging operations in the redwood forests of Northern California.

The company that took over Pacific Lumber is known as Maxxam Group, wholly owned by Maxxam, Incorporated, a conglomerate controlled by Charles Hurwitz of Houston, TX. It is well-known that at the time of the takeover, Hurwitz made clear his intention to terminate the pension plan so he could use the excess pension funds to help pay for the leveraged buyout. Accordingly, in March 1986, the Hurwitz-controlled Pacific Lumber Company board of directors voted to terminate the pension plan and to purchase a group annuity contract to pay for the plan's benefits.

During this same time period, Hurwitz was assisted by Drexel Burnham Lambert, who issued $450 million in junk bonds to raise funds for the Pacific Lumber buyout. And incidentally, Executive Life purchased 45 percent of this $450 million in junk bonds.

In September 1986, prior to Pacific Lumber's selection of an insurance company to provide the group annuity, Pacific Lumber's then vice president of finance, Vince Garner, warned the plan fiduciaries against purchasing the group annuity from Executive Life because, as he concluded among other things, it was excessively laden with junk bonds, had suspicious accounting and reinsurance practices, and was certainly perceived poorly by employees.

Furthermore, professional consultants hired by Pacific Lumber Company to give advice about an annuity provider echoed Mr. Garner's warnings.

Nevertheless, on October 1, 1986, Charles Hurwitz and other Pacific Lumber officers selected Executive Life to provide the group annuity to pay plan benefits. Pacific Lumber paid Executive Life, who was the lowest bidder, $37.2 million for the group annuity, which was just $2.7 million less than they could have paid and gotten the group annuity with Metropolitan Life Insurance Company.

After doing that, Pacific Lumber Company and Maxxam Group recaptured $62 million in plan assets. What they could have done, for example, had they selected Metropolitan Life for an additional $2.7 million, instead of this high-risk Executive Life, they would have paid $39.9 million for the group annuity and still had for their reversion for their purpose, for whatever they wanted to use it, over $59 million in plan assets.

Later on, Pacific Lumber Company sold off all these cutting and welding subsidiaries, including Pacific Lumber, in 1988, leaving Pacific Lumber with only the redwood logging operations in Northern California. And in September 1989, a group of people there, plan members and beneficiaries, brought suit in Federal court in San Francisco, alleging that Hurwitz and other plan fiduciaries had breached their ERISA fiduciary duties because they selected Executive Life, even though there were many indications that Executive Life was financially unsound and feeling that they did it because they were just trying to get maximum return out of the plan for their own use.

On April 11, 1991, unfortunately—or fortunately, as the cases may be—the State of California seized Executive Life, which had been swamped by defaults in its enormous junk bond portfolio. Since its seizure, Executive Life has paid retirement benefits due under the group annuity contract at the rate of 70 cents on the dollar. For example, from Executive Life, my monthly benefit for the service I put in with Victor fell from $562 to $393 a month. A co-plaintiff, Paul Brady's, monthly benefit fell from $254 to $177 a month. The only other income he has is about $800 from Social Security.

Many retired Victor employees saw their benefits drop below $100 a month as a result of this action. At that time, what was perceived as a major concern became a potential disaster. So we in Texas contacted the law firm in Oakland represented here today so we could become directly involved in this process.

Following Executive Life's seizure, retirees of Pacific Lumber's main company in the logging area picket the headquarters. They were obviously quite upset. And after Executive Life went under, Pacific Lumber agreed for the 1 month of May 1991 to make up the 30 percent differential for those people in Northern California.

However, down in Texas, we did not picket; we did not use that method, but there was letter writing and petition signing, and there was a great deal of consternation over this. When approached, Pacific Lumber refused to make any differential payments to the retirees of Victor Equipment Company and other cutting and welding subsidies because, as Maxxam's corporate counsel told one of my co-plaintiffs, Jim Lovell, and I quote, "Maxxam felt no obligation toward the retirees of the cutting and welding companies because those companies were no longer a part of Pacific Lumber or Maxxam."

Maxxam ignored the fact that the cutting and welding retirees were just as much plan participants as were the logging company retirees. And Pacific Lumber Company refused to commit at that time to making differential payments, even for the logging retirees, beyond the May 1991 month.

The law firm of Sigman & Lewis, the plaintiffs' attorneys who, at our request represented Victor plan members, negotiated with Maxxam to force it to make these differential payments to the cutting and welding retirees and not just to the logging retirees, and furthermore, to make a commitment to keep making those payments.

Now, it was during this time that I joined the lawsuit as a plaintiff—and incidentally, this was the first time I had ever been either

a plaintiff or a defendant in any lawsuit, so I did not take this lightly. Several Victor associates who were on limited income during this time, very limited income, contributed $5, $10 and $25 for the cause because they wanted to be involved in this.

In January 1993, we won a ruling from the judge that the selection of an annuity provider was a fiduciary act governed by ERISA. On May 11, 1993, we proved that the defendants, Charles Hurwitz and William Leone, who was president of Pacific Lumber, were plan fiduciaries when they selected Executive Life. Through this ruling, Al tells me, based on this, Hurwitz and Leone are personally liable for all losses attributable to the fiduciary breaches.

However, the bad news is that the next week, the judge threw our case out of court, ruling that my co-defendants and I were only "former participants" in a terminated plan, and therefore we had no right to sue even though Pacific Lumber Company unilaterally selected a financially unsound insurance company and acted out of self-interest, not plan participants' interests. And there we go back to this Catch-22 situation.

I personally am incensed and discouraged, not only for myself, but for the many hundreds of people that I know have been similarly affected, not only in Victor, but in Pacific Lumber Company. We can no longer count on the courts the way it stands now for the redress that we thought was guaranteed under ERISA. We see no permanent solution as long as Executive Life or a successor has our annuities.

It certainly wasn't comforting to read, as I did earlier this year in the Wall Street Journal, the headline, "Executive Life Bailout Springs Big Leak." And there have been articles in BusinessWeek and others, indicating that this is no solution.

Our lawsuit sought to permanently guarantee through the purchase of a group annuity from a reputable insurance company—and going back to what you asked Secretary Berg, we are only asking that we be made whole so that we have guarantees that for the balance of our lives—and bear in mind that many of our people aren't even going to start drawing retirement benefits for another 5 or 10 or 15 years, because of their age, so many of them are going to be dependent upon this being in place many, many years from now—and that no plan participants will ever lose any retirement benefits, and that Hurwitz and other fiduciaries be held accountable for selecting a financially unsound insurance company.

I know I speak on behalf of my co-plaintiffs and other plan participants and beneficiaries when I strongly urge you —and I praise you for the legislation—to urge you to see it through Congress and to make absolutely clear that plan participants can, even after a pension plan has been terminated, bring suit if that is necessary for breaches of fiduciary duty so long as they were participants of the breach.

Al Sigman has allowed me to use his time, and he is here today to answer any legal questions you might have following the panel's presentations. Just by way of background, Mr. Sigman is an expert in ERISA, having served on the ERISA Advisory Panels in both the Carter and Reagan administrations, and in 1981, as one of former Labor Secretary Donovan's representatives on an interagency task force which examined ERISA 10 years after its enactment. Mr.

Sigman also represented the plaintiffs before the U.S. U.S. Supreme Court in the Mertens v. Hewitt case, and he has taken his first vacation in many years since that decision. I am sure he would be happy to respond to any questions you might have about what we are talking about.

We need your help, we appreciate what you are doing, and we ask that Congress ask right away. Thank you very much.

[The prepared statement of Mr. Miller follows:]

Prepared Statement of Jack Miller

I. INTRODUCTION

I am a retired former employee of Victor Equipment Company, in Denton, TX, outside Dallas. Victor Equipment Company formerly was owned by the Pacific Lumber Company. As an employee of Victor, I was a participant in the Pacific Lumber Company Retirement Plan which was terminated effective March 31, 1986. Despite my status as a plan participant, a Federal judge on May 17, 1993 held that I and seven other Plan participants lack standing under ERISA to sue for breach of GSA fiduciary duty. The judge ruled that I am only a former participant of a terminated pension plan and therefore lack standing, although my lawsuit concerned alleged breaches of fiduciary duty made in the course of terminating the Plan.

when I read the Judge's ruling throwing my case out of court, I realized that her reasoning left participants and beneficiaries like me stranded. Under her ruling, pension plan fiduciaries could avoid any liability for admitted breaches of fiduciary duties simply by terminating a pension plan. Once the plan was terminated, participants and beneficiaries could do nothing about the fiduciary breaches, no matter how blatant, willful or harmful those breaches were to the participants and beneficiaries.

So, despite the fact that lawsuits by participants and beneficiaries for breaches of fiduciary duty are intrinsic to ERISA's enforcement scheme, and despite the fact that Congress intended ERISA to provide ready access to Federal court to protect the interests of participants in their pension plans, this Federal judge, as have other courts, construed ERISA so narrowly that Congress' intentions have been substantially undermined.

You should note, too, that the situation my co-plaintiffs and I face is not unique. There are numerous lawsuits pending around the country by participants like me whose pension plans were terminated to recapture excess surplus as part of a corporate reorganization or buy-out; and who receive retirement benefits from and Executive Life Insurance Company group annuity. (Executive Life was taken over by the State of California as insolvent in April, 1991.) Some of these lawsuits concern the pension plans of National San, RJR/Nabisco, Revlon, and Cannon Mills—the biggest of the corporate takeovers in the 1980's. In all these actions, a court could easily conclude that the participants of a terminated pension plan lack standing under ERISA and throw those cases out of court.

II. THE ALLEGATIONS OF FIDUCIARY MISCONDUCT

In order to demonstrate why the judge's ruling has such a devastating impact on participants and beneficiaries, and why it undermines the enforcement I think Congress envisioned, I would like to explain to you some of the factual background to the lawsuit.

I worked at Victor for 14 years. Before retiring, I was personnel director there. Presently, I am retired and consult on a part time basis. I also serve as a city councilman in Denton. I am married, and have 2 children at home.

I became involved in this litigation in 1991, following the collapse of Executive Life Insurance Company and the resulting reduction of my monthly pension from Executive Life. The retirement benefits I earned from Pacific Lumber are paid through an Executive Life group annuity; which is the subject of my lawsuit. Because of my former position at Victor, I know a lot of the Victor employees who were in the Pacific Lumber pension plan.I communicate fairly regularly with a dozen or so retired Victor employees, and provide them with information about the lawsuit against Pacific Lumber for the retirees' pensions and about the condition of Executive Life. Because Denton is a relatively small town, news travels fast to several hundred Plan participants who are still working at Victor.

In late 1985 and early 1986, the Pacific Lumber Company (which still owned my employer, Victor Equipment) was taken over in a highly leveraged takeover. At that

time, Pacific Lumber owned a number of subsidiaries, in locations from San Diego to Texas to New Hampshire, including Victor, my employer. These subsidiaries manufactured products for metal cutting and welding; we called them the cutting and welding subsidiaries. The employees of the cutting and welding subsidiaries were Plan participants just as the employees of Pacific Lumber's logging operations.

Pacific Lumber was taken over by Maxxam Group, Inc., which is owned by Maxxam, Inc., which is a natural resources conglomerate owned by Charles Hurwitz. As part of the takeover, Hurvitz planned to terminate the Plan so that he could recapture excess pension assets. So, in March, 1986, the Hurwitz-controlled Pacific Lumber board voted to terminate the Plan and to purchase a group annuity contract to pay the benefits due from the Plan.

Meanwhile, in the course of raising capital to take over Pacific Lumber, Hurwitz, assisted by Drexel Burnham Lambert, issued $450 million in junk-bonds; Executive Life purchased 45 percent of the junk bonds.

In September, 1986, in the course of Pacific Lumber's selection of an insurance company to provide the group annuity, Pacific Lumber's vice president for finance and treasurer, Vince Garner, warned that Executive Life was laden with junk bonds, had suspicious accounting and reinsurance practices, and was perceived poorly by employees because of its role in Hurwitz' takeover of Pacific Lumber. Mr. Garner's warnings echoed those of professional consultants Pacific Lumber had hired for advice about an annuity provider. Nevertheless, on October 1, 1986, Charles Hurwitz and other Pacific Lumber officers, selected Executive Life to provide the group annuity to pay Plan benefits. Pacific Lumber paid Executive Life, the lowest bidder, $37.2 million for the group annuity, $2.7 million less than the next lowest bid of Metropolitan Life. After purchasing the group annuity, Pacific Lumber recaptured $62 million dollars in surplus plan assets. Obviously, Pacific Lumber would have recaptured $2.7 million less if it had selected Met Life.

Later, Pacific Lumber sold off all of cutting and welding subsidiaries, and the only company left is the Pacific Lumber Company—the logging company. Victor Equipment was sold-off in 1988.

In September, 1989 a number of participants and beneficiaries brought suit in Federal court in San Francisco, alleging that Hurwitz and other Plan fiduciaries had breached their ERISA fiduciary duties because they selected ELIC even though they should have known it was not financially sound and to maximize the amount of Plan assets Pacific Lumber would recapture.

On April 11, 1991, the State of California seized ELIC, which had been swamped by defaults in its enormous junk bond portfolio. Since its seizure, ELIC has paid only 70 percent of retirement benefits due pursuant to the group annuity contract. My monthly payment fell to $368 from $562. My co-plaintiff, Paul Brady's monthly annuity payment fell from $254 to $177; Mr. Brady's only other income is his Social Security check of about $800.

Following ELIC's seizure, retirees of Pacific Lumber's main company, the logging company, picketed corporate headquarters. As a result, Pacific Lumber agreed to pay, for May 1991, the difference between ELIC's payments and those actually due as retirement benefits. However, down in Denton, at the Victor Equipment plant, there was no picketing, although there was a lot of letter-writing and petition-signing. Pacific Lumber, however, refused to make any differential payments to retirees of the cutting and welding subsidiaries because, as Maxxam's corporate counsel told my co-plaintiff, Jim Lovell, "Maxxam felt no obligation toward the retirees of the cutting and welding companies—because those companies were no longer a part of Pacific Lumber or Maxxam;" Maxxam ignored the fact that the cutting and welding retirees were just as much Plan participants as were the logging company retirees. Pacific Lumber also refused, at that time, to commit to making the differential payments for the logging retirees beyond May, 1991. Fortunately, the 1989 lawsuit was pending, and the plaintiffs' attorneys negotiated with Maxxam to force it to make differential payments to the cutting and welding retirees as Maxxam had to the logging retirees, and to make a commitment to keep making those payments. In Denton, our group of cutting and welding retirees sighed with relief. After that, I joined in the lawsuit as a plaintiff.

In June, 1991, the Secretary of Labor filed a lawsuit against Pacific Lumber and Maxxam, alleging the same breaches of fiduciary duty as we had alleged.

In January, 1993, we won a ruling from the judge that the selection of an annuity provider was a fiduciary act governed by ERISA, and not a "plan sponsor" act free from ERISA's fiduciary standards.

On May 11, 1993, we proved that defendants Charles Hurwitz and William Leone (Pacific Lumber's president) were Plan fiduciaries when they selected Executive Life. This ruling, my attorneys tell me, subjects Messrs. Hurwitz and Leone to personal liability for all losses attributable to the fiduciary breaches. The next week,

the judge threw our case out of court because my co-plaintiffs and I were only former participants in a terminated plan; therefore we had no right to sue because Pacific Lumber picked a lousy life insurance company in order to enrich itself.

Even though cutting and welding retirees are now receiving their fully monthly benefits from a temporary patch-work of Executive Life, the insurance industry (who pitched in to help with Executive Life's insolvency) and Pacific Lumber, the future of Executive Life is not certain. Our lawsuit, however, sought to guarantee permanently that no Plan participants would ever lose any retirement benefits just because Hurwitz, and other fiduciaries picked a financially unsound insurer for their own benefit, and to the detriment of me and all the Plan's participants and beneficiaries.

Therefore, I know I speak on behalf of my co-plaintiffs and the other Plan participant and beneficiaries when I strongly urge you to approve the proposed legislation that makes it clear that participants such as myself can, even after a pension or employee benefit plan has been terminated, bring suit for breaches of fiduciary duty, so long as they were participants at the time of the breach. Thank you.

Senator METZENBAUM. Thank you very much, Mr. Miller. I have a couple questions, but one that I am unclear about is you say that, "On May 11th, we proved that defendants Charles Hurwitz and William Leone were plan fiduciaries when they selected Executive Life. This ruling, my attorneys tell me, subjects them to personal liability." Then the Court threw the case out a week or two later. I am not quite clear—what was the original ruling, Mr. Sigman?

Mr. SIGMAN. There were a series of motions that the judge heard seriatim over a period of weeks, and the earlier motions, as Mr. Miller described them, dealt with fiduciary status and whether or not Mr. Hurwitz, despite the fact that he was not designated in the formal plan instrument as a fiduciary, whether or not as a result of the discretionary control and authority that he wielded regarding the plan, the judge agreed with us and the Department of Labor that he was in fact a fiduciary, subject to the fiduciary standards of the Act.

It was following that ruling that the judge ruled in favor of Mr. Hurwitz' motion at a subsequent hearing, which knocked my clients out of the litigation on the grounds that they had no standing, despite our prior success with regard to that motion establishing Hurwitz' fiduciary status, and despite the fact that under threat of a motion for preliminary injunction, Mr. Hurwitz and his colleagues caved in and in effect have stipulated to a de facto preliminary injunction requiring them to maintain the status quo during the pendency of the litigation.

We are now in limbo. We don't even have the legal authority to enforce that stipulation.

Senator METZENBAUM. Is that Court ruling on appeal now?

Mr. SIGMAN. Yes, it is.

Senator METZENBAUM. Mr. Miller, I suspect the Pacific Lumber takeover and Executive Life bankruptcy has been quite stressful for you and your family. How much has the termination of your pension plan and the default of your annuity affected your own personal retirement security?

Mr. SIGMAN. In terms of up to this point, it hasn't. Because of Mr. Sigman's efforts, we have been able to get the 30 percent from Pacific Lumber, and now there is some type of patchwork thing put together, so we still get 100 percent. However, our concern is that this is just a stopgap measure. I hope to live many, many years, and what is going to happen if this thing is not corrected? That's number one. And number two, I have many friends whose pension

benefits are considerably less than mine, and they are much more dependent on it for their sole income than am I. And they worry constantly that if what could happen up to now has happened, that this unknown, this uncertainty, that the worst will happen in the future, at the time when they need it the most. These are people who may be in their sixties and seventies. So there is a tremendous amount of mental anguish out there among people whose benefits, by our standards, are quite small, but who depend upon this to be able to keep things together.

Mr. SIGMAN. Our position legally, if I may add briefly, is that Mr. Miller and the other former participants of this plan are entitled to the matter of the remedy that we seek to either a backup annuity, a full replacement annuity from a strong company such as Metropolitan Life Insurance Company or some other major carrier, or at least a backup annuity which would kick in in the event there are further problems with Executive Life Insurance Company.

And I would add that the legislation which you and Senator Kassebaum have introduced, according to my reading of it, would assure that that remedy is available. And that is not all that clear as of today, because Mr. Hurwitz and his colleagues argue that since the plan has been terminated and because under ERISA, as interpreted by the courts, the type of relief we are seeking can only run to the plan—in other words, Mr. Miller presently, even if he had standing, would not have the right to sue for an individual benefit to make up the difference between what he is entitled to under the terms of the terminated plan and what he may get as a result of however the conservatorship winds up.

What we are seeking is at least a backup annuity which would kick in, and we also believe that it should be clear under ERISA that it is the obligation of the breaching fiduciary, if we establish in court that in fact they breached their fiduciary duty in making the selection of Executive Life, to go out and purchase that backup annuity so that my clients don't have to in their retirement sit back and worry day to day about what is going to happen, and whether or not that retirement money is going to be there.

I think one thing that this legislation would do, and I think it is vitally important that it be passed as quickly as possible, would be to assure that that remedy would be available, and that the Federal courts would have the power to order the defendants who breach their fiduciary duty to go out and spend their own money to purchase either a full replacement annuity or a backup annuity.

Senator METZENBAUM. Senator Kassebaum.

Senator KASSEBAUM. Mr. Chairman, I am sorry. We have the nominations on the floor that Senator Wellstone spoke of, and they are asking me to come over and speak as well, so I may have to leave. But you please just go ahead and know that our purposes are joined in this effort.

I appreciate the testimony, and I have been reading through some of the other testimony as well, and I appreciate everyone coming.

Senator METZENBAUM. Thank you, Senator Kassebaum. And I appreciate all your help.

Mr. Miller, do you think retirees should have a say in whether an insurance annuity is being purchased for them and with which insurer it is purchased?

Mr. MILLER. I think there should be some input, yes. Now, I realize it is a long, involved decision, but I think that should be part of the decisionmaking process, yes.

Senator METZENBAUM. Mr. Sigman, do you happen to know how much, in connection with the purchase, involved actual real assets, and how much involved good will when Pacific Lumber took over this company?

Mr. SIGMAN. No, I can't respond to that.

Senator METZENBAUM. Let us go on to the next witness. Ms. Vicki Gottlich, staff attorney with the National Senior Citizens Law Center in Washington, DC. We'd be pleased to hear from you.

I did not invoke the 5-minute rule with respect to the other witnesses, but those of you who are now speaking are well-acquainted in the Washington area, and you understand our 5-minute rule, so if you could hold your testimony to that time, I'd very much appreciate, but we'll be rather lenient.

Ms. GOTTLICH. As a New Yorker, I'll talk as quickly as I can to get the most into my 5 minutes.

Senator METZENBAUM. No, please, don't talk that rapidly. Just take your time.

Ms. GOTTLICH. I want to thank you for the opportunity to testify here today. The National Senior Citizens Law Center provides litigation and technical support to legal services programs funded by the Legal Services Corporation and the Administration on Aging. That means that our clients and those of the attorneys we assist are primarily elderly and primarily poor.

We have been working on pension issues since 1973, when the program first began, and we intend to continue helping retirees and workers receive their pension and health benefits. That is why the modest proposals in your legislation under consideration are very important to us and to our clients.

I want to point out how important pension income is for low-income individuals. If clients receive incomes from pensions, it can prevent them from living in poverty. Some of our clients have had their incomes double after we have been successful in helping them attain their pension benefits. In one dramatic case, we had clients who were homeless and were able to secure places to live after we successfully got them their pensions. That is a very dramatic change.

It also means for us, because our clients live so close to the edge, they require their pension benefits. If something happens to their benefits, and they are reduced even by 30 percent, that can mean the difference between living in poverty and being able to have a better income.

We have also noticed that the lack of pension income is a particularly important factor for women and for people of color. Recent studies have pointed out things that we have already seen, that is, that poor women who are divorced live in poverty if they don't have pensions; if they have pension incomes, they are better able to live a life that is closer to their former middle income status.

In order to receive pensions, however, plan participants and retirees must be able to enforce their rights under the plan. Participants have not been able to do this effectively because of the limited remedies under ERISA. The Mertens case has actually limited these remedies even further; thus, we would like to see a greater expansion of the remedies available to participants.

It is too bad that Senator Kassebaum has left, because I wanted to assure her that the remedies proposed by you and Senator Kassebaum in your legislation really are not an expansion of the remedies that we seek and that we think are necessary under ERISA; they really only bring participants to the place where they were before the Mertens decision was issued.

When I testified before this committee before, I have talked about ways to expand remedies. I will not do that today because I really want to emphasize what you and Senator Kassebaum and assistant secretary Berg have said, that these remedies are really very limited.

The inability to use traditional remedies really hurts plan participants, and without trust remedies they are going to be hurt even further. Many times, it is not enough to just restore benefits due when benefits have been reduced by plan mismanagement, or by willful fiduciary violations. We have had clients who have not been able to pay their mortgages while waiting for their benefits. One the get their benefits, they have income, but many times, they have lost their houses, so they really are not made whole. And there is nothing in this bill that would make them whole or that would restore the lost house to them or compensate for that particular damage.

We have also found that workers are discouraged from bringing suits to enforce their rights because of the lack of remedies available. If you are suing to address a fiduciary breach for the plan, for example, and you may not necessarily get an increase in your benefits, it is a difficult suit to bring because you may not have the money to bring that suit—and our clients very often don't have the money to bring that suit. But yet, if nobody is challenging the fiduciary breach, then the plan itself is being hurt, and fiduciaries may be unjustly enriched.

There is also very little to deter the pension plan from continuing to violate ERISA, and that is especially true if they are dealing with nonfiduciaries. A nonfiduciary who just has to return a fee may not be as concerned about participating in a fiduciary breach as they would be if they had to assist in repayment of the make-whole remedy.

The problem that we have seen quite often, though, is the problem of lack of standing. We have had several instances where we have had clients who were former participants in a plan. They may have received an annuity after the termination of a plan, or they may have received a lump sum distribution. The annuity may have been an Executive Life type annuity, which is not paying them the full benefit to which they are entitled, or we have had incidents where clients received their lump sum, only to discover that the plan may have improperly calculated their benefits. And yet the courts have determined that they are no longer participants with

standing to sue under the plan because they do not have the right to sue under the plan.

For our clients, this has limited the availability to receive the money which they are due, or to protect their future rights to benefits under the plan. And again, since our clients depend so heavily on the pension benefits in order to escape poverty, this is really a drastic blow to them.

We appreciate your efforts in this area to restore the situation before Mertens, and we look forward to providing whatever assistance we can.

Thank you.

[The prepared statement of Ms. Gottlich follows:]

PREPARED STATEMENT OF VICKI GOTTLICH

Thank you for the invitation to testify concerning the proposed amendments to the Employee Retirement Income Security Act (ERISA) that would increase the remedies available to participants and retirees who do not receive the pension benefits to which they are entitled.

The National Senior Citizens Law Center provides litigation and technical support to legal services programs funded by the Legal Services Corporation and the Administration on Aging. Our clients and those of the legal workers to whom we provide assistance are primarily low-income and elderly. From the time that it was organized in the early 1970's, the Law Center has helped workers and retirees receive their pension and health benefits. That is why the modest proposals under consideration today are important to us and to our clients.

Receipt of pension benefits can make a dramatic difference in the life of the older clients we represent. If clients receive income from pensions in addition to their social security, they may live in modest comfort rather than in poverty. Some of our clients' incomes have doubled after we successfully helped them obtain their pensions. Even more dramatic, class members who were homeless were able to afford places to live as a result of our establishing their right to receive pensions in the class action, Ponce v. Construction Laborers Pension for So. Cal., Trust, 774 F.2d 1401 (9th Cir. 1985).

The lack of pension income is a major factor contributing to the higher poverty rates among elderly women and minorities. For example, a recent report on the economic status of divorced older women found that poor divorced older women were less likely to have pensions than those divorced older women do not live in poverty. Schultz, J., The Economic Status of Divorced Older Women, (1993). This supports the observations we have made, based on our clients' experiences, about the importance of pensions to the well-being of older persons.

If pension plan participants and retirees are to receive their benefits and the full protection of ERISA, they must be able to enforce their rights under their plans and under the law. Participants have not been able to do this effectively because of the limited remedies provided under ERISA. Thus, the relief available to participants under ERISA must be expanded in order to encourage private enforcement and to ensure that participants receive the pensions they earned.

Three years ago, in July 1990, I had the opportunity to come before this Committee and suggest ways in which ERISA could be improved to benefit those for whom its protections were designed. Today I will focus on only one small portion of the issues involved in ERISA enforcement reform, the issue of remedies. I will discuss separately the effect of ERISA's limited remedies on benefits claims and breach of fiduciary duty claims, beginning with benefit claims.

ERISA currently allows participants or beneficiaries to sue to recover benefits due under the plan, to clarify rights to future benefits under the plan, to enjoin a plan practice which violates ERISA, or to obtain other equitable relief to redress violations or enforce ERISA. 29 U.S.C. Sec. 1132(a). The only monetary award available, other than payment of benefits due, is the discretionary penalty for failure to comply with ERISA notice and disclosure requirements. 29 U.S.C. Sec. 1132(c). Punitive and other extra contractual damages are generally not available. Massachusetts Mutual Life Insurance Co. v. Russell, 105 S.Ct. 3085 (1985).

Unfortunately for participants and beneficiaries, ERISA supersedes all State laws, with the exception of those concerning banking, insurance, or criminal matters. 29 U.S.C. Sec. 1144. ERISA pre-emption has been interpreted very broadly by the courts, so that State laws which provide alternative causes of action for ERISA pro-

tected benefits are not available to litigants. For example, claims of breach of contract, fraud, infliction of emotional distress, tort, vexatious delay in processing claims, bad faith, and deceptive trade practices have been held to be preempted.

The inability to use traditional tort and contract claims for monetary damages hurts plan participants and the enforcement process in a variety of ways. First, there is no relief *or most of the injuries caused by a plan's failure to comply with ERISA or the terms of the plan. It often is not enough to restore benefits due, especially when the benefits have been reduced by plan mismanagement or willful fiduciary violations. A retiree who cannot pay the mortgage because his pension was wrongfully withheld may eventually receive his benefits, but he may not receive them in time to prevent the foreclosure of his mortgage. Yet ERISA provides no compensation for the loss of his home.

Second, many workers are discouraged from bringing suit to enforce their rights by the lack of remedies available. The benefit they will recover may be too small to make the costs of litigation rewarding. Now many people, especially low-income workers, would spend $5,000 litigating a suit to recover $2,000 in wrongfully denied pension benefits? But if they do not litigate, the plan may deny other workers their benefits, and be unjustly enriched by money that rightfully belongs to the participants. If the worker could recover damages for the delay in processing his claim, or for bad faith or fraud, he may reconsider his decision not to enforce his rights.

Finally, there is little to deter a pension plan from continuing to violate ERISA, even after suit is brought. A damage award in favor of a participant and against the plan and fiduciaries would make many plans rethink some of their actions. Courts should also be permitted to award punitive damages to plan participants, although such awards should be limited to the most egregious breach of fiduciary duty cases, or ERISA Section 510 claims.

Although ERISA provides remedies for breach of fiduciary duty, many courts have held that they are only available to make the plan, and not the plan participants, whole. In other words, a plan participant can sue a fiduciary under 29 U.S.C. Sec. 1109 to recover plan assets but not to recover the benefits that he or she may have lost due to the breach of fiduciary responsibility. The problem frequently arises in connection with misrepresentations made by fiduciaries and with distributions from a profit-sharing plan For example, a legal services lawyer sought assistance for a client whose plan improperly delayed distribution of his benefits until a time when their value was decreased due to an investment loss. Although the delay may have been the result of a fiduciary breach, the client may have no claim against the fiduciary for the reduction in his anticipated pension. Thus, ERISA provides no protection for participants and retirees whose benefits are reduced by fiduciary conduct in violation of the statute. At the very least, they should be allowed to recover from the fiduciaries for the direct losses incurred as a result of the fiduciary breach.

The problem of remedies is complicated by the narrow interpretation given by Federal courts to the question of who has standing to bring a claim under ERISA for a fiduciary breach. Generally, actions for relief under 29 U.S.C. Sec. 1109 may be brought by the Secretary of Labor, a participant, beneficiary, or a fiduciary. 29 U.S.C. Sec. 1132(a) (2). In order to be a participant or beneficiary, the plaintiff must be entitled to benefits under the plan. Individuals who have already received the benefit the plan claims is due them under the plan may be denied standing to challenge the actions of the fiduciary in arriving at that benefit, even if the fiduciary engaged in misconduct.

A recent decision in the United States District Court for the Northern District of California provides a good example of the problem. Plaintiffs challenged the action of the plan fiduciaries in terminating their pension plan, taking a $55 million reversion to finance a leveraged buy-out of the company, and purchasing annuities for participants and retirees with the Executive Life Company. Plaintiffs allege that the fiduciaries chose Executive Life, despite recommendations by consultants and actuaries that annuities be purchased from another company, because they saved one and a half million dollars by accepting Executive Life's bid, and because a large portion of the junk bonds financing the buy out were purchased by Executive Life. when Executive Life experienced difficulties, the value of plaintiffs' annuities was jeopardized, and the plaintiffs sought protection for their annuities against possible future losses. Yet the District Court ruled that the plaintiffs lacked standing because the plan has been terminated, the plaintiffs have received the annuities, and they are not eligible to receive benefits from the plan. Kayes v. Pacific Lumber, No. C-89-3500 SBA (Order filed May 17, 1993). While Secretary of Labor Reich's suit against the Pacific Lumber Company remains, it will not provide the plaintiffs in the Kayes case with the remedy they seek. If ERISA enabled participants to obtain relief against fiduciaries for reductions in their benefits resulting from fiduciary breaches, the plaintiffs would not be left without a remedy.

Equally problematic for participants is the inability to seek redress against nonfiduciaries, i.e. professionals such as attorneys, accountants, actuaries who provide services to plans. The U.S. Supreme Court in Mertens v. Hewitt Associates, 61 U.S.L.W. 4510 (June 1, 1993) recently foreclosed the possibility of bringing suits for monetary damages against nonfiduciaries who knowingly participate in fiduciary breaches, finding nothing in the language of ERISA that would support such suits. Yet the misconduct of these nonfiduciaries may effect participants and beneficiaries as adversely as the misconduct of fiduciaries. Plans may be terminated and/or benefits reduced as a result of misconduct and malpractice by attorneys, actuaries, and accountants. Employers acting in their corporate, rather than fiduciary, capacity may mislead employees or break promises about benefits due. Yet plan participants are left without means to redress their grievances because of the limited redress available under ERISA.

The legislation under consideration addresses only a few of the problems raised in my testimony. While it is but a modest proposal, it will benefit a substantial number of participants and retirees who are without recourse to obtain the full amount of benefits to which they are due.

I applaud this first step to increase individual enforcement of ERISA, and look forward to continuing to work with the Labor Committee on ways to address the additional problems I have raised.

Senator METZENBAUM. Thank you very much, Ms. Gottlich.

What is the National Senior Citizens Law Center, and how is it funded?

Ms. GOTTLICH. We are a legal services backup corporation. That means we receive money from the Legal Services Corporation to provide assistance to legal services lawyers and pro bono lawyers who represent low-income individuals. We also receive funding form the Administration on Aging and also from private sources of income. For example, we currently have our Retirement Research Foundation money to investigate some pension issues pertaining to women.

Our clients are primarily low-income, and I want to point out to you that for a low-income individual, it is very difficult to get representation in a pension case. There are probably three Legal Services programs out of the 1,200 across the country that actively do ERISA litigation. There are a few more that will do it if pushed. So for low-income individuals, even if you restore the law before Mertens, it doesn't necessarily mean there is going to be a push toward increased litigation or increased remedies. All it means is that those few low-income individuals who are able to find an attorney to assist them will get the remedies; it will not increase the litigation that they bring.

Senator METZENBAUM. Is all of your work done pro bono?

Ms. GOTTLICH. Yes, it is. We are entitled to receive attorneys' fees if they are awarded to us under some of our ERISA litigation and some of our other litigation.

Senator METZENBAUM. Thank you very much. We appreciate your testimony, and I do have a couple of questions for you.

Do you think the pension system generally works well for those who are covered by it, or is the abuse in the system widespread?

Ms. GOTTLICH. It is very hard for a lawyer to answer those questions because we only see the bad cases. So I surmise that there are a lot of good plans going out there, but we also see a lot of abuse. We have dealt with a lot of issues that are not before us today concerning prevention of people vesting. We have seen many instances of people not getting their pension plan distribution in a timely manner in accordance with the terms of the plan. But again, we only see the abuses; we very often don't see the good points.

Senator METZENBAUM. Would our pension system be more protective and responsive to workers and retirees if workers and retirees were more involved in how the plans are run?

Ms. GOTTLICH. Yes. I think it definitely needs more involvement by participants and retirees. I think ERISA started in the right direction by its disclosure provisions, but it hasn't really gone far enough.

Senator METZENBAUM. In your opinion, why shouldn't individuals have the full range of remedies available to them under ERISA?

Ms. GOTTLICH. I think they should have a full range of remedies available to them. I know there has been a concern about the effect upon plan stability, and we see a lot of termination of defined benefit plans. I can't see where an increase in remedies would really increase the litigation that much, and I can't really see that it would bring that much damage to the stability of the pension system.

Senator METZENBAUM. As I understand, today the law is that if an individual is able to sue a plan fiduciary, that when he or she finally collects, maybe 2 to 5 years later, after the court holds the fiduciary liable, all that the pensioner would receive would be the actual amount of damages and nothing in excess of that, so the fiduciary has no special obligation to see to it that the claims are paid.

Ms. GOTTLICH. I think that is correct. After 5 years of litigation, all you are going to get is the benefits that were due you 5 year previously. It does not take into account, for example, back pay if you were terminated before you vested, or other kinds of remedies.

Senator METZENBAUM. Thank you very much.

Mr. Vine, a partner at Covington and Burling, on behalf of the ERISA Industry Committee, we are happy to have you with us, sir.

Mr. VINE. Thank you, Senator, and good morning.

My name is John Vine. I am a partner in the firm of Covington and Burling, and I am counsel to the ERISA Industry Committee, commonly known as ERIC. I appear before you today on ERIC's behalf.

ERISA currently gives the government, participants and beneficiaries a broad array of remedies to recover damages from fiduciaries who have violated their duties and to enable participants and beneficiaries to recover benefits they are due.

However, ERISA is not just a remedial statute. Employee benefit plans are voluntary arrangements, and ERISA is designed to encourage employers to provide benefits voluntarily to their employees. It does to by protecting employers from unnecessary litigation and excessive and unintended liabilities.

ERIC is deeply concerned that any amendments to ERISA's enforcement provisions will be both unnecessary and harmful to the employees and employee benefits that Congress intends to protect. Legislation that stimulates more litigation will reduce, not increase, the benefits that employees receive under our Nation's voluntary employee benefit system.

ERIC does not believe there is any need to change ERISA's enforcement provisions. If the subcommittee approves any changes, the legislation should be narrowly tailored to meet specific, clearly demonstrated needs. Sweeping changes in ERISA's enforcement

provisions are likely to have severe adverse effects on employees, their families, and the benefits they receive.

The U.S. Supreme Court's Mertens decision is a narrow one. It does not alter the arrange of remedies that the Labor Department, participants and beneficiaries have against fiduciaries. It does not diminish their ability to recover benefits that have been wrongfully denied to recover damages to a plan caused by a fiduciary breach, to recover any gains improperly made by a fiduciary, or to invoke traditional equitable remedies such as injunction, mandamus and restitution. It does not impair the ability of a fiduciary to make any breach of contract, tort, malpractice, or other claim it might have against a service provider with whom the fiduciary contracts.

In appropriate circumstances, a fiduciary could be obligated by ERISA to make these claims and could be ordered by a court to pursue them. Mertens cut back on none of these remedies.

The Kayes and Novak cases are lower court decisions. It is wholly premature for the Congress to respond to them before the judiciary has had a full opportunity to resolve the issues that these cases raise.

As for the Executive Life situation, it is not clear that any employee will lose benefits in the rehabilitation of Executive Life. Current indications are that the rehabilitation plan will provide for a full or nearly full recovery for most participants.

In view of the narrow scope of S. 1312 and the strong interest of the chairman, the ranking minority member and other members of the subcommittee in the bill, ERIC can support it. However, ERIC's support is based on its understanding of the bill's purpose and effect, that it does not alter ERISA's standards of fiduciary responsibility; that it applies only if there is a purchase of an annuity in connection with the termination of an individual status as a covered participant in a pension plan, and that the only participants entitled to sue under the bill are those for whom annuities have been purchased. We ask the subcommittee to clarify each of these points.

ERIC has serious reservations about the bill's retroactive effective date. ERIC is willing to go along with retroactivity in the context of this particular bill, but feels strongly that retroactivity should be the rare exception and not the rule.

Finally, ERIC would strongly object to any expansion of the bill. Although ERIC can support S. 1312 because it is narrowly written, ERIC will strongly oppose any efforts to expand it.

I thank the chairman and the members of the subcommittee for the opportunity to testify. I will be happy to respond to any questions you have.

Thank you.

[The prepared statement of Mr. Vine follows:]

PREPARED STATEMENT OF JOHN M. VINE

Mr. Chairman and members of the subcommittee, good morning. My name is John Vine. I am a partner in the law firm of Covington & Burling. I am counsel to the ERISA Industry Committee, commonly known as ERIC, and I appear before you today on ERIC's behalf.

THE ERISA INDUSTRY COMMITTEE

The ERISA Industry Committee is an association of more than 120 of the Nation's largest employers concerned with national retirement and welfare benefit issues. As the sponsors of pension, savings, health, disability, life insurance, and other welfare. benefit plans covering millions of participants and beneficiaries, ERIC's members share with this subcommittee a strong interest in the success and expansion of the employee benefit plan system in the private sector.

VOLUNTARY EMPLOYEE BENEFIT PLANS

Major employers provide pension, savings, health, disability, life insurance, and other important benefits to their employees through voluntary employee benefit plans. Although employers are not required to provide benefits to their employees, voluntary employee benefit plans have been remarkably successful in delivering needed pension and welfare benefits to millions of employees and their families and dependents. Over 80 percent of the employees in the private sector receive employee benefit plan coverage.

The vast majority of employee benefit plans are well-funded, well-managed, and entirely successful in delivering promised benefits to employees and their dependents. The vast majority of employee benefit plans are operating soundly. There is no reason to believe that a significant number of plans are being mismanaged or that a significant number of employees are failing to receive the benefits they are due.

It is, of course, extremely regrettable when any employee fails to receive the benefits he or she is due, whether because of mismanagement or because of economic circumstance. ERISA was designed to respond to these problems, and under current law, appropriate remedies are available to address them.

ERISA is not just a remedial statute, however. It also is designed to encourage employers to provide benefits voluntarily to their employees. It provides this encouragement by protecting employers from unnecessary litigation and excessive and unintended liabilities.

ERIC is deeply concerned that any amendments to ERISA's enforcement provisions will be both unnecessary and harmful to the employees and employee benefits the legislation is intended to protect and encourage. Legislation that stimulates more litigation will reduce, not increase, the benefits that employees receive under our Nation's voluntary employee benefit system.

If the subcommittee approves any legislation, the legislation should be narrowly tailored to meet specific, clearly demonstrated needs. Sweeping changes in ERISA's enforcement provisions are likely to have severe adverse effects on employees, their families, and the benefits they receive.

THE IMPACT OF LITIGATION ON VOLUNTARY BENEFITS

Employee benefit plans are voluntary arrangements: employers are not required to provide benefits to their employees. As a result, an employer's decision to provide benefits to its employees is heavily influenced by the costs it expects to incur in providing those benefits.

In an increasingly competitive and fragile economic environment, employers cannot afford to maintain benefit plans that expose them to potentially huge and unpredictable costs. If the costs of maintaining benefit plans are high or unpredictable, employers are unlikely to adopt new plans; mounting costs are likely to persuade employers to cut back on their existing plans and to terminate many of them altogether.

Litigation can impose staggering and unpredictable costs on employers. I refer not merely, or even primarily, to the potential for damage awards. The cost of litigation itself is staggering. Even litigation that has no merit can be extremely costly. Many cases are driven to settlement, not because of the merits of the case, but because the cost of litigation is so high.

Legislation that increases the potential for litigation is thus likely to be counterproductive: by increasing employers' litigation costs, the legislation will discourage the formation, continuation, and expansion of employee benefit plans. Employers will be required to budget, and allocate to litigation costs, funds that they otherwise would allocate to benefits.

Litigation is a costly, inefficient, and haphazard way of assuring that plans are properly administered and that employees receive the benefits to which they are entitled. Experience in other areas, such as medical malpractice, has taught us that more litigation can disrupt the provision of benefits and services, and that it too often becomes part of the problem rather than part of the solution.

It is with this in mind that we urge the subcommittee to proceed cautiously and to evaluate carefully and critically any proposals to alter ERISA's existing enforcement provisions. Congress adopted those provisions deliberately, after taking into account both the need to protect participants and beneficiaries and the need to encourage employers to provide benefits voluntarily.

Before making any changes, the subcommittee should carefully consider whether existing law provides adequate protection to participants and beneficiaries. ERIC believes that it does.

In our judgment, existing law already gives both the Government and plan participants and beneficiaries an ample array of remedies to punish miscreants, to recover damages from fiduciaries who have violated their duties, and to enable participants and beneficiaries to recover the benefits they are due.

CURRENT CRIMINAL AND CIVIL SANCTIONS

Under current law, the Department of Justice, the Department of Labor, and the Internal Revenue Service already have at their disposal a broad array of criminal and civil sanctions to enforce ERISA. The criminal sanctions include penalties for such conduct as theft, embezzlement, bribes, kickbacks, misrepresentation, concealment of facts, failure to comply with ERISA's reporting and disclosure obligations, and coercive interference with a participant's exercise of his rights under ERISA. The civil sanctions include fines, penalties, and severe adverse tax consequences for violations of ERISA's reporting and disclosure obligations, its funding and fiduciary responsibility standards, its participation, vesting, and coverage requirements, and the health care continuation and Medicare secondary payer provisions.

Plan participants and beneficiaries can sue to recover any benefits they have been wrongfully denied. And both they and the Department of Labor can sue to require plan fiduciaries who have violated their fiduciary duties to make good to the plan any losses it incurred as a result of the breach or to remit to the plan any profits the fiduciary has wrongfully made through the use of plan assets. A fiduciary that has breached its fiduciary duties also is subject to any other equitable or remedial relief that a court may deem appropriate.

RECENT COURT DECISIONS

The Department of Labor has expressed concern about several recent court decisions. Chief among them are the U.S. Supreme Court's decision in Mertens v. Hewitt Associates, the district court decision in Haves v. Pacific Lumber, and the Eighth Circuit's decision in Novak v. Andersen. I would like to review briefly what the courts held in each of these cases.

Mertens. As I mentioned earlier, plan fiduciaries are subject to a wide array of legal and equitable remedies to enforce ERISA's fiduciary responsibility standards. ERISA defines the term "fiduciary" broadly to include any person who exercises discretion or control over the assets, management, or administration of a plan. The U.S. Supreme Court held in Mertens that the equitable relief that is available under ERISA does not include money damages. In dictum, the Court also questioned, but did not decide, whether a plan participant has a cause of action under ERISA against someone who is not a plan fiduciary.

Mertens does not alter the array of remedies that the Department of Labor and plan participants and beneficiaries have against plan fiduciaries under ERISA. Mertens does not diminish in any way their ability to sue to recover benefits that have been wrongfully denied, to recover any damages to a plan that are caused by a fiduciary breach, to recover any gains made by a fiduciary as a result of a fiduciary breach, or to invoke such traditional equitable remedies as injunction, mandamus, and restitution. Nor does Mertens impair the ability of a fiduciary to make any breach of contract, tort, malpractice, or other claims it might have against a service provider with whom the fiduciary contracts. In appropriate circumstances, a fiduciary could be obligated by ERISA to pursue these claims, and could be ordered by a court to pursue them.

Mertens cut back on none of these well established-remedies. In Mertens, the Court decided only the very narrow issue of whether money damages are an available form of equitable relief when a participant or beneficiary sues a nonfiduciary service provider under section 502(a) (3) of ERISA.

Kayes. While Mertens was decided by the U.S. Supreme Court, Kayes was decided by a trial court, the U.S. District Court for the Northern District of California. In Kayes, the district court held that former participants and beneficiaries to whom a plan had discharged its benefit obligations by distributing annuity contracts do not have standing to sue the plan's fiduciaries under Title I of ERISA.

Kayes does not alter in any way the Labor Department's authority to pursue its pending lawsuits against plan fiduciaries who purchased Executive Life annuities without complying with ERISA's fiduciary duties. As far as the standing of participants is concerned, Kayes is not a final judgment. The court's decision is subject to review, and possible reversal, by the Ninth Circuit Court of Appeals and, perhaps, by the U.S. Supreme Court.

The possibility of reversal on appeal might not be just a theoretical point: the Ninth Circuit has granted an expedited appeal in Kayes. In other circumstances (Amalgamated Clothing & Textile Workers Union v. Murdock), the Ninth Circuit has ruled that a former participant may bring a suit under ERISA. It remains to be seen whether the Ninth Circuit will follow this approach in Kayes.

Novak. In Novak, the Court of Appeals for the Eighth Circuit addressed an entirely different issue: whether "make-whole" remedies are a form of equitable relief under section 502(a)(3)(B) of ERISA. The plaintiff in Novak had participated in an employee stock ownership plan and had received full distribution of his account balance under the plan. The plan's administrators had failed, however, to notify him that he could avoid immediate tax on plan distributions by rolling them over within 60 days into an IRA.

The plan required the plan's administrators to distribute all legally required notices, including the rollover notice required by section 402(f) of the Internal Revenue Code. The plaintiff conceded, however, that he had received all of the benefits to which he was entitled under the plan; he did not argue that the damages he sought were a part of the benefit offered by the plan.

In view of the plaintiff's concession that he had received all of the benefits he was entitled to under the plan, the Eighth Circuit held that he could not recover his lost tax benefits under the rubric of "appropriate equitable relief." The court recognized that its decision was inconsistent with the Sixth Circuit's decision in Warren v. Society National Bank.

In Warren, a plan participant alleged that the trustee of two retirement plans violated the terms of the plans by failing to distribute all of the funds due to him in a single calendar year. The participant sought damages as compensation for the resulting loss of tax benefits. The Sixth Circuit held that such damages were available under section 502(a) (3) of ERISA.

The U.S. Supreme Court denied the plaintiff's petition for certiorari in Novak. In its amicus brief, the Government recommended that the Court not grant plenary review of the case, and suggested that if the Court were to affirm the Ninth Circuit's decision in Mertens (as it later did), the Court might wish to deny the petition for certiorari in Novak and await further developments. The Court followed the Government's recommendation when it denied certiorari in Novak. As a result, because of the conflict between Novak and Warren, the issue will require further attention by the courts before it is finally resolved.

In sum, of this group of cases, the only one decided by the U.S. Supreme Court (Mertens) was an extremely narrow decision that did not cut back on any of the well-established remedies that ERISA provides. The other two cases (Haves and Novak) were very recent decisions that addressed issues which will also be addressed by other district and appellate courts, and perhaps ultimately by the U.S. Supreme Court. Since the Kayes case is still pending, and since other courts have reached different conclusions, it is too soon for anyone to draw firm conclusions on the basis of Kayes and Novak. In our judgment, therefore, it is both premature and unnecessary for Congress to enact legislation in reaction to Kayes and Novak.

THE EXECUTIVE LIFE SITUATION

Because of the limited significance of the recent court decisions, ERIC does not believe that legislation is required to respond to them. The significance of the recent court decisions in the context of the Executive Life situation is even more limited.

First, it is not clear that any employee will lose any portion of his or her retirement benefits in the rehabilitation of Executive Life:

—Active and deferred vested employees have not been affected by the Executive Life rehabilitation.

—Most annuitants are currently receiving their full retirement benefits under the court-supervised rehabilitation.

—The California Insurance Commissioner submitted a revised rehabilitation plan to the court on April 20. Although concerned parties are still reviewing the revised rehabilitation plan, current indications are that the plan will provide a full or almost full recovery for the majority of plan participants.

Second, employers have acted responsibly throughout the rehabilitation of Executive Life:

—A group of employers formed the Committee of Companies Concerned for the Annuities of Retired Employees ("CoCare ") to assure that retired workers would receive the maximum possible recovery from the Executive Life rehabilitation proceedings. From the outset, CoCare has closely monitored the rehabilitation proceedings in order to protect employees retirement income.

—When the California Insurance Commissioner temporarily reduced annuity payments to 70 percent of the level specified in the Executive Life policies, many employers voluntarily made up the missing amounts.

—ERISA's prohibited transaction provisions actually make it difficult for employers to adopt remedial measures in the Executive Life situation. Despite these difficulties, a number of employers have sought to relieve their plans of any risk associated with the Executive Life rehabilitation. The Department of Labor has received dozens of applications for prohibited transaction exemptions from employers who wish to provide "make whole" payments to plans that hold contracts issued by Executive Life and other troubled insurers.

As I will explain, the real problem in the Executive Life situation is the inadequacy of State insurance regulation, not any deficiency in ERISA enforcement. In the majority of cases, there is no basis for a claim that the employer breached its fiduciary duty under ERISA when it purchased Executive Life annuities:

—Nearly all of the employers who purchased Executive Life annuities did so at a time when Executive Life held the highest possible rating from all three of the major rating agencies (Moody's, Standard & Poor's, and A.M. Best & Company). These ratings indicated that Executive Life had demonstrated the strongest ability to meet its policyholder and other contractual obligations. The rating agencies had far more information about the financial condition of Executive Life and other insurers than private employers could hope to obtain; there was no reason for employers to second-guess the experts' assessment of Executive Life's financial strength.

—Employers who purchased Executive Life annuities for terminating pension plans did so under the supervision of the PBGC, and in accordance with the procedures specified in the PBGC's regulations. Under the PBGC's own rules, these employers fully discharged their benefit obligations to plan participants.

—When the Executive Life annuity purchases were made, there was no indication that employers should follow a prescribed procedure in selecting an annuity provider. Indeed, even today neither the PBGC nor the Department of Labor has been able to articulate a regulatory standard that it considers appropriate. Most employers who purchased Executive Life annuities acted prudently in light of the information available at the time, and in the absence of guidance from the regulatory agencies.

—The vast majority of Executive Life cases do not involve allegations that fiduciaries engaged in self-dealing or other misconduct when they purchased Executive Life annuities. In the few cases where there was clear evidence of misconduct, the Department of Labor has already had ample opportunity to pursue claims on behalf of the affected plans. The Department has, in several instances, already recovered monetary damages for these plans.

As I have explained, the Department of Labor and plan participants and beneficiaries have adequate remedies under existing law:

—Section 409 of ERISA expressly provides that any fiduciary who breaches his duty is liable to make good any losses to the plan, and that the fiduciary is subject to any other equitable or remedial relief that a court deems appropriate. Under section 502(a) (2) of ERISA, either a fiduciary or a participant may invoke this provision to recover monetary damages on behalf of a plan from a fiduciary that breached its duty by purchasing an Executive Life annuity. The Department of Labor has asserted claims under section 502(a) (2) in its pending Executive Life cases; nothing in the U.S. Supreme Court's Mertens decision would affect these claims.

—I am not aware of any Executive Life case in which either the Department of Labor or a participant has sought to recover monetary damages from a nonfiduciary on the theory that the nonfiduciary knowingly participated in a fiduciary breach. To the extent that the U.S. Supreme Court's decision in Mertens casts doubt on the availability of a remedy against a nonfiduciary, it does not affect pending Executive Life cases.

Where plaintiffs have been unsuccessful in litigating Executive Life cases, their lack of success has had nothing to do with the Mertens decision. Instead, the cases have been resolved in favor of defendants because they failed to show that the defendants breached their duty to the plan or its participants, or because, as in Kayes, the plaintiffs failed to show that they had standing to pursue an ERISA claim.

To the extent that the Executive Life rehabilitation has revealed problems that require a legislative solution, the problems do not lie with ERISA enforcement. In-

stead, the problems lie with the inadequacy of State insurance regulation that led to the failure of Executive Life:

—ERISA expressly reserved to the states the power to regulate the insurance industry.

—Employers, like other consumers, are entitled to rely on the assumption that the companies from which they purchase insurance products are receiving adequate oversight from State regulators.

—To hold that employers must guaranty the annuity obligations of insolvent insurers defeats the purpose of insurance in this context: to shift risk from a federally regulated employee benefit plan to a state-regulated insurer. If an employer cannot discharge its benefit obligations under a plan by purchasing insurance from a company licensed by the State, the employer cannot, as a practical matter, ever truly terminate a defined benefit plan.

We have conducted a preliminary review of S. 1312, the "Pension Annuitants Protection Act of 1993," which is intended to provide relief to plan participants for whom annuities have been purchased. Because the bill was introduced only last Thursday, my comments on the bill are necessarily preliminary. ERIC may wish to make additional comments in the future, as its staff and its members continue to analyze the bill.

The bill provides that if (1) there is a purchase of an insurance contract or insurance annuity in connection with the termination of an individual's status as a participant in a pension plan with respect to all or part of the participant's pension benefit and (2) the purchase violates either ERISA's fiduciary standards or the terms of the pension plan, the Department of Labor or a participant, beneficiary, or fiduciary may sue under ERISA to obtain "appropriate relief, including the posting of security if necessary, to assure receipt by the participant or beneficiary of the amounts provided by such insurance contract or annuity, plus reasonable prejudgment interest." The bill applies to any legal proceeding pending or brought on or after May 31, 1993.

For the reasons I have presented here this morning, ERIC believes that ERISA's existing array of remedies adequately protects the interests of participants and beneficiaries, and that a legislative response to the recent decisions in Mertens, Kayes, and Novak is unnecessary and premature.

However, in view of the narrow scope of S. 1312, and in view of the strong interest of the Chairman, the ranking minority member, and the other members of the subcommittee in addressing this narrow subject, ERIC can support the bill.

ERIC's support for the bill, however, is based on its current understanding of the bill's purpose and effect.

First, we understand that the bill does not alter in any way ERISA's standards of fiduciary responsibility. We understand that the phrase "other than the relief authorized in section 2 of this Act" in section 4 of the bill is intended only to make clear that section 2 permits the Department of Labor and certain participants, beneficiaries, and fiduciaries to obtain relief, and not to alter the duties of the plan's fiduciaries.

Second, we understand that the bill applies only if there is a purchase of an insurance contract or insurance annuity in connection with the termination of an individual's status as a participant covered under a pension plan. For example, the bill will not apply where a pension plan purchases a guaranteed interest contract from an insurance company solely for purposes of investment.

We also understand that the participants entitled to sue under the bill are only those participants for whom annuities have been purchased in connection with the termination of their status as participants covered under a pension plan. For example, the bill does not allow a participant for whom an annuity has not been purchased to bring an action under ERISA. This follows from the relief that the bill would provide: "appropriate relief—to assure receipt by the participant or beneficiary of the amounts provided by such insurance contract or annuity.

In order for ERIC to support the bill, it is very important that the subcommittee clarify each of these points.

ERIC is concerned about the bill's retroactive effective date. ERIC generally opposes retroactive changes in the nontax provision of ERISA, and it therefore has serious reservations about the retroactive provisions of this bill. However, ERIC understands that, in the particular circumstances created by the Executive Life cases, the bill's sponsors have concluded that there is a need for retroactivity, and ERIC is reluctantly willing to go along with the bill's retroactive effective date. ERIC feels strongly, however, that retroactivity should be the rare exception, not the rule, and that the subcommittee should not regard the bill's retroactive effective date as a precedent for legislative action in the future.

Finally, ERIC would strongly object to any expansion of the bill. As I have explained, ERIC feels strongly that amendments to ERISA's enforcement provisions are unnecessary and likely to be counterproductive. Although ERIC is willing to support S. 1312, because it is so narrowly written, ERIC will strongly oppose any efforts to expand it.

ERIC is particularly concerned about efforts to amend ERISA to allow plaintiffs to recover open-ended extra contractual or consequential damages. Making employers and plan fiduciaries liable for open-ended damage awards will create an avalanche of length and costly litigation and is likely to result in a substantial cutback in the benefits that employers provide to their employees.

Any expansion of the remedies available under ERISA will harm the millions of employees and family members who are covered by voluntary employee benefit programs.

This completes my prepared statement. I wish to thank the Chairman and the members of the subcommittee for the opportunity to testify. I will be pleased to respond to any questions that the Chairman or the members of the subcommittee might have.

Senator METZENBAUM. Thank you very much, Mr. Vine.

I think we'll hear from Mr. Klein, executive director of the Association of Private Pension and Welfare Plans, and then have questions for the two of you together.

Please proceed.

Mr. KLEIN. Good morning, Senator Metzenbaum.

I am James Klein, executive director of the Association of Private Pension and Welfare Plans, APPWP. I am accompanied today by Ted Rhodes, a partner with the law firm of Steptoe and Johnson, and our general counsel.

As you know from the numerous occasions on which my organization has had the privilege to testify before the Senate Subcommittee on Labor, the APPWP's members either sponsor directly or provide services to pension and health care plans that cover more than 100 million Americans. As you also know, Senator Metzenbaum, on each of those previous occasions when we have testified before this subcommittee, we have regretted the necessity of stating our opposition to what you were at the time advocating. It is a real pleasure, therefore, to have at least this one opportunity before you retire to come here and compliment you for proposing a narrow, precise response to a particular perceived problem. I am sure that neither one of us ever thought the APPWP would have this opportunity.

Senator METZENBAUM. There is going to be a brass band coming in very shortly to celebrate the occasion. [Laughter.]

Mr. KLEIN. OK. Approximately 6 weeks ago, our association was one of more than 80 companies and organizations which formed a coalition in response to efforts here in the Senate to attach to the Omnibus Budget Reconciliation Act a sweeping and very detrimental legislative proposal. That proposal not only would have hastily and unwisely repealed the U.S. Supreme Court's recent decision in Mertens v. Hewitt Associates, but also would have greatly expanded the scope of liability for fiduciaries and nonfiduciaries under ERISA. Fortunately, due to the efforts of many both inside and outside the Congress, but especially thanks to Senator Kassebaum, action on that ill-advised legislation was halted.

While I had planned to devote my testimony today almost exclusively to S. 1312, the Pension Annuitants Protection Act, legislation which we believe can only fairly be read to address narrow issues such as those arising out of the Executive Life Insurance cases, I

do feel compelled to mention at least in passing that I am troubled by language in your floor statement, Senator Metzenbaum, accompanying the introduction of S. 1312 and by some of the other comments I heard earlier today, suggesting that S. 1312 is needed because of the Mertens decision. We should be clear—S. 1312 in no way limits the sound ruling in Mertens.

Just last week, the coalition I referred to a moment ago testified before the House of Representatives' Labor-Management Relations Subcommittee on the broader issues concerning the Mertens decision and fiduciary and nonfiduciary liability. A copy of the coalition's written testimony before the House is attached as an appendix to my statement today and should suffice for today as my formal comments on the need to preserve the result in Mertens, and I do understand that it will be included as part of the official hearing record.

Senator METZENBAUM. Without objection, it will be included.

Mr. KLEIN. Today, though, I want to focus more narrowly on S. 1312, which appears to be designed to address specific problems which the Department of Labor believes arise in connection with the Executive Life cases. We do not necessarily believe that the Department's concerns are well-founded regarding the unavailability of certain remedies in these cases. In addition, since the workout of the estate of Executive Life is not yet complete, it is not yet clear how many, if any, annuitants will not receive their full promised benefits.

It is worth nothing that information supplied by the National Organization of Life and Health Guaranty Associations indicates that through the various State guaranty associations, approximately 93 percent of the 86,400 participants for whom Executive Life annuities were purchased will receive 100 percent of their monthly benefits. For those who may receive less than 100 percent, actions under ERISA if a fiduciary breach is proven may provide a complete recovery. Of course, for those who may not receive their full promised benefit, the shortfall is a real problem, and we have heard very good testimony to that effect this morning from Mr. Miller. But overall, it would appear that the provisions intended to protect participants, both State guaranty funds and ERISA have worked well.

Because S. 1312 was introduced just 4 days ago, we are not in a position to support this liberalization today. We believe, and we re sure you would agree, that the best way to legislate, especially when amending a complex and carefully crafted statute like ERISA, is to follow a thoughtful and deliberative review. Nevertheless a committee of the APPWP has on an expedited basis reviewed the issue of remedial legislation to clarify the law with regard to the purchase of an annuity in a plan termination. It is this committee's vie that if there is legal uncertainty regarding the ability to recover the benefits actually loss, ERISA might be amended to provide for such a specific recovery. While there remains some uncertainty whether such recovery of benefits is currently available, S. 1312 appears to limit itself to the recovery that the APPWP committee considered appropriate, and for this we commend you. We will next take up this matter with our board of directors for its review.

In the very brief period we have had to look at your legislation, we have identified a number of matters that concern us. These concerns are spelled out more fully in my written statement, and I won't go into them in depth in these few moments of oral remarks. Just briefly, though, I would want to mention that our concerns include the lack of clarity regarding whether the bill is intended to permit a recovery only for lost benefits or for an anticipated loss; also, what distinction is intended between an insurance contract and an insurance annuity. In addition, further language may be needed to clarify that plan sponsors do not have liability arising out of an action taken by others after annuities are purchased.

Finally, we strongly oppose retroactive legislation which creates new burdens and obligations on plan sponsors' expectations. A litany of burdensome new requirements, many of them imposed upon plan sponsors retroactively, have exacted a toll in plan terminations and a dismal record of new plan establishments. Nevertheless, we recognize that unless the clarification proposed in S. 1312 is adopted retroactively, it may not serve its basic purpose, since many of the Executive Life cases have already been initiated.

Moreover, because we view this proposed legislation as a clarification rather than as establishing new liabilities, there is a potential basis for not opposing its retroactivity in this narrow instance.

In conclusion, I want to compliment you for your efforts in fashioning a precise and targeted response to issues rising out of the Executive Life litigation, you may count on our sincere dedication in working with you to seek a response that meets both your concerns as well as our concern that legislation not be adopted that would make more difficult the challenges employers already face in sponsoring retirement plans for their workers.

Thank you very much.

[The prepared statement of Mr. Klein follows:]

Prepared Statement of James A. Klein

Good morning Chairman Metzenbaum, Senator Kassebaum and members of the subcommittee. I am James A. Klein, Executive Director of the Association of Private Pension and Welfare Plans (APPWP). I am accompanied today by Theodore Rhodes, a partner with the law firm Steptoe & Johnson and General Counsel for the APPWP. As you know from the numerous occasions on which my organization has had the privilege to testify before the Senate Subcommittee on Labor, the APPWP's members either sponsor directly or provide services to pension and health care plans that cover more than 100 million Americans. Accordingly, our members have a keen interest in legislation that affects the responsibilities of those who sponsor and operate the voluntary employee benefit plan system that is essential for the retirement income security and health care coverage needs of American workers, retirees and their families.

Just last week a coalition, of which the APPWP is a member, testified before the House of Representatives Labor-Management Relations Subcommittee on issues arising out of the U.S. U.S. Supreme Court decision in Mertens v. Hewitt Associates, 113 S. Ct. 2063 (1993), and fiduciary and nonfiduciary liability. A copy of the coalition's written testimony before the House of Representatives is attached as an appendix to my statement today.

Today, I want to take the opportunity to discuss legislation aimed at perceived problems concerning certain individuals whose pension annuities were purchased from the Executive Life Insurance Company, prior to its financial failure.

S. 1312, the "Pension Annuitants Protection Act of 1993", introduced last week, by Senators Metzenbaum and Kassebaum appears to be designed to address specific problems which the U.S. Department of Labor believes arise in connection with litigation related to the failure of Executive Life. The APPWP does not necessarily believe that the Department of Labor's concerns are well-founded regarding the un-

availability of certain remedies in the Executive Life cases. In addition, the "workout" of the estate of Executive Life is not complete and it is not yet clear how many, if any, annuitants of Executive Life will not receive their full, promised benefits.

By way of background it is worth noting that information supplied by the National Organization of Life and Health Guaranty Associations (NOLGHA) indicates that through the various State guaranty associations, approximately 93 percent of the 86,400 participants for whom Executive Life annuities were purchased will receive 100 percent of their monthly benefits. Those participants not fully covered will receive at least 77 percent of their monthly benefits from the estate of Executive Life and from State guaranty funds. The amount could be higher depending on the outcome of separate litigation that may benefit the estate of Executive Life. In addition, for those who may receive less than 100 percent of their monthly benefits, actions under ERISA, if a fiduciary breach is proven, may provide a complete recovery. Of course, for annuitants who may not receive their full promised benefit, the shortfall is a real problem. But, overall, it would appear that the provisions intended to protect participants—state guaranty funds and ERISA—have worked well.

We realize that the Department of Labor, and some in Congress, wish to address certain issues in anticipation of a less than satisfactory resolution of the Executive Life "workout", or possible legal impediments faced in connection with Executive Life litigation. That desire to resolve the potential problems is the impetus for S. 1312 and I would, therefore, like to focus the remainder of my remarks on the specifics of that legislation.

Because S. 1312 was introduced just 4 days ago, the APPWP is not in a position to support this legislation today. There simply has not been adequate time to follow our procedures for review and approval. Nevertheless, a committee of the APPWP has reviewed the issue of remedial legislation to clarify the law with regard to litigation involving the purchase of an annuity in plan termination. It is this committee's view that if there is legal uncertainty regarding the ability to recover the benefits actually lost and not recovered through applicable State insurance guaranty funds, or voluntary employer/sponsor arrangements, ERISA might be amended to provide for such a specific recovery. That view has not been passed upon by our Board of Directors and, therefore, is not official APPWP policy. While there remains some uncertainty whether such recovery of benefits is currently available, S. 1312 appears to limit itself to the recovery that the APPWP committee considered appropriate, and for this we commend you. We pledge to pursue this matter with our Board of Directors, and we look forward to working with the Congress and the Department of Labor in fashioning a response that is mutually satisfactory to the executive and legislative branches of government and to our members.

In the brief period we have had to review S. 1312 we have identified a number of matters that concern us. First, it is unclear whether the bill is intended to permit a recovery only for lost benefits, or whether it is possible for a recovery to be based on an anticipated loss—without taking into account the actual amounts recovered under a State guaranty fund. Second, section 2 of the bill refers to the purchase of "an insurance contract or insurance annuity in connection with the termination of an individual's status as a participant". It is unclear in what circumstances there would be a purchase of an insurance contract as opposed to the purchase of an annuity in the event of a termination of participation. Accordingly, we believe any reference to insurance "contract" should be deleted unless it can be satisfactorily explained what purpose it serves.

We are also concerned that the bill language may need to be more precise in referring not only to the purchase of an insurance annuity in connection with the termination of an individual's status as a participant, but also at the time of such termination. Absent such a clarification, the APPWP might be concerned about any implication that plan sponsors may have any liability arising out of an action taken by others at some time after annuities were purchased for the benefit of pension plan participants.

Finally, of great concern to the APPWP is the retroactive nature of the legislation. We strongly oppose retroactive legislation which creates new burdens and obligations on plan sponsors' expectations in adopting employee benefit plans, and undermines the voluntary employee benefit system. A litany of burdensome new requirements, many of them imposed upon plan sponsors retroactively, have exacted a toll in plan terminations and a dismal record of new plan establishments. We urge Congress to avoid the temptation to enact retroactive legislation that discourages the sponsorship of plans.

Nevertheless, we recognize that unless the clarification which is proposed in this legislation is adopted retroactively it may not serve its fundamental purpose of assuring that there will be an opportunity to recover losses incurred, if a fiduciary breach can be demonstrated, since many of the cases have already been initiated.

Moreover, because we view this proposed legislation as a clarification rather than establishing new liabilities, there is a potential basis for not opposing its retroactivity in this narrow instance.

In conclusion, we wish to compliment Senators Metzenbaum and Kassebaum for your efforts in fashioning a precise and targeted response to the perceived problems arising out of Executive Life litigation. The Congress and the Department of Labor can count on the APPWP's sincere dedication to working with you to seek a response that meets both your concerns as well as our concern that legislation not be adopted that would make more difficult the challenges employers already face in sponsoring retirement plans for their workers. Thank you.

Prepared Statement of Charles Kamen

Good morning Mr. Chairman, my name is Charles Kamen and I am Executive Director, Human Resources for U.S. West. With me is Ted Rhodes, a Partner at Steptoe and Johnson. I am here today on behalf of a coalition of over eighty entities. The group is comprised of major employers, insurers, actuarial firms and a variety of trade associations who are interested in maintaining the vitality of the private retirement system and ensuring that participants and beneficiaries receive promised benefits.

We are pleased to discuss the Mertens v. Hewitt decision with you.

The Department of Labor has outlined its concerns about the U.S. Supreme Court's decision in Mertens v. Hewitt. I would like to address three areas with you. They are: (1) the Senate Labor and Human Resources' amendment to the Senate's Budget Reconciliation Bill which purported to address these concerns;(2) why the Mertens decision should stand; and (3) the purported connection of the Mertens decision to on the Department's lawsuits involving plan sponsors who purchased Executive Life annuities.

Before addressing these three areas, I would like to briefly recap for the subcommittee the events that followed the announcement of the Mertens decision on June 1—less than 2 months ago.

At the Department's request, Senator Metzenbaum introduced an amendment to the Labor Committee's Budget Reconciliation legislation that allegedly addressed only the holding in Mertens. On June 16, scarcely 2 weeks after the Mertens decision and without any hearings or other consideration, Senator Metzenbaum's amendment was approved by the Senate Labor Committee by a 9–8 vote.

While purporting to merely overturn the U.S. Supreme Court's June 1 decision in Mertens v. Hewitt, the legislation in fact went far beyond that. Mertens held that equitable relief for violations of ERISA does not include money damages. However, service providers remain liable for traditional equitable relief, such as restitution of fees and profits. Further, fiduciaries also remain fully liable under Section 409 of ERISA to injured plan participants.

Despite the significant remedies available under ERISA even after the Mertens ruling, the Metzenbaum amendment would have expressly provided for nonfiduciaries to be jointly and severally liable with fiduciaries to plans and participants for knowing participation in a fiduciary breach. Remedies for such breaches were expanded to include compensatory and arguably punitive damages. And the proposal applied retroactively, permitting pending suits to come under these new provisions.

The Coalition believes that Congress should not rush to judgment in matters involving ERISA especially in the case of the proposed amendment which was so expansive, dramatically altering the liability and remedies provisions under ERISA. Accordingly, the coalition was firmly of the view that before any action was taken, consideration should be given to the overall impact the legislation would have on our Nation's employee benefit system. Evidently, this point rang true for on July 23, hours before passage of the Budget Reconciliation legislation by the Senate, Senator Metzenbaum withdrew his amendment.

I believe it is worthwhile to review the legislation introduced on behalf of the Department of Labor. The legislation sought by DOL would:

—amend section 502(a) of ERISA to make ambiguous settled law that precludes punitive damages in ERISA cases;

—amend ERISA section 502(a) to expand the damages that can be recovered against plan sponsors, fiduciaries, and nonfiduciaries to include the "full economic value" (a new and undefined term) "of any benefits participants and beneficiaries would have received absent such violations"—remedies would no longer be limited to lost benefits;

—expand the classes of individuals entitled to sue under ERISA section 502(a) to include former participants and beneficiaries;

—amend ERISA section 409 to make nonfiduciaries jointly and severally liable for breaches by fiduciaries, making the nonfiduciaries potentially liable for actions over which they have no control;

—amend ERISA section 501(l) to significantly expand ERISA's current civil penalties; and

—permit suits on the basis of the bill's new provisions for conduct that occurred before the enactment of the bill.

These changes are sweeping, and would result in being costly to plan sponsors, and not in the best interests of plan participants and beneficiaries. In enacting ERISA, Congress carefully weighed the costs and benefits involved in devising the law's enforcement and remedies provisions. A reasoned decision was made regarding the costs of an enforcement and damages scheme on plan sponsors and service providers including any possible benefits to be gained. Any attempt to upset the carefully crafted balance in ERISA without a comprehensive review of its effects would be inappropriate in light of the Administration's proposal to overhaul the Nation's health care system which will inevitably include extensive ERISA revisions.

WHY THE MERTENS DECISION SHOULD STAND

ERISA established appropriate statutory rules that govern the activities of those who deal with an employee pension benefit plan. The cornerstone of ERISA is whether an individual or entity is a "fiduciary" under the statute. ERISA requires that fiduciaries be personally liable to a plan for any money the plan loses due to a breach of statutory duties. The definition of fiduciary is very broad and includes any individual who exercises discretionary control or authority over a plan's management, administration or assets. The remedies available against fiduciaries who breach their fiduciary duties are equally broad, covering both compensatory damages to the plan and a full panoply of equitable relief.

In Mertens the U.S. Supreme Court concluded that equitable relief available to plan participants and beneficiaries for violations of ERISA by any party (including plan fiduciaries) does not include money damages.

Maintaining ERISA's existing enforcement rules does not mean that plan participants are without redress for breaches of fiduciary duty. Under ERISA, plan participants have extensive rights of redress against plan fiduciaries, who must exercise their duties for their exclusive benefit. As part of that duty, employee benefit plan fiduciaries must continually monitor the activities of nonfiduciaries (e.g., accountants, actuaries,insurance companies) that they hire, and are obligated to take appropriate action if nonfiduciaries are not carrying out their functions appropriately.

As recognized by the U.S. Supreme Court in its opinion "exposure to [unlimited nonfiduciary] liability would impose high insurance costs upon persons who regularly deal with and offer advice to ERISA plans, and hence upon ERISA plans themselves." Indeed, if nonfiduciaries were exposed to unlimited liability, such potential exposure would lead to increased costs, which would ultimately be passed on to plan participants in the form of reduced benefits. Such exposure is particularly severe and unwarranted because nonfiduciaries by definition have no control over the actions ultimately taken on behalf of a plan by plan fiduciaries. As the U.S. Supreme Court recognized, the current ERISA enforcement scheme "allocates liability for plan-related misdeeds in reasonable proportion to respective actors' power to control and prevent the misdeeds."

The ramifications of overturning Mertens go far beyond the issue of nonfiduciary liability for damages. The decision addresses the broader issue of whether ERISA authorizes the recovery by participants and beneficiaries of money damages under its equitable relief provisions for any violation of ERISA by any party.

While my testimony has concentrated on employee pension benefit plans, ERISA also provides the rules under which health care plans operate. Since the legislation to overturn Mertens would apply to health care plans as well as pension plans, it would seriously undermine national health care reform efforts. A centerpiece of the health care reform proposal being developed by the Administration is a greater reliance upon efforts to ensure quality, appropriate care at an affordable cost but this legislation would impose significantly greater liabilities upon fiduciaries and service providers who must make the decisions about appropriate care under the terms of the health plan.

Overturning Mertens would dramatically extend the relief available generally under ERISA. That, in turn, would substantially increase the costs of managing and administering all ERISA employee pension and welfare benefit plans. ERISA was primarily crafted, after 10 years of difficult negotiating effort, as a delicate balance of employer and participant interests to ensure the future of the private employee

benefit system. Without an in-depth analysis of the impact of any potential changes, that balance may be upset to the detriment of plan participants and beneficiaries.

The Effect of the Mertens Decision on the Department's Lawsuits Involving Plan Sponsors Who Purchased Executive Life Annuitants

It is essential to underscore that the Mertens decision has nothing to do with the typical Executive Life case brought by the Department. In Mertens, the Court addressed the liability of a nonfiduciary service provider under ERISA Sec. 502(a) (3) in an action brought by plan participants alleging knowing participation in a fiduciary breach. Without deciding whether ERISA allows participants to sue on these grounds, the Court concluded that any such liability under Sec. 502(a) (3) did not include money damages, i.e., legal relief, but was instead limited to traditional equitable relief and remedies, such as injunctions or restitution. Thus, the Mertens decision was an extremely narrow ruling, limited to the scope of available relief under Sec. 502(a) (3) alone.

In contrast, the typical Executive Life case involves claims against plan fiduciaries, charging them with imprudence and other fiduciary misconduct for buying Executive Life annuities with plan assets in connection with a plan termination. In accordance with ERISA's comprehensive civil enforcement scheme, claims of this nature against plan fiduciaries are asserted under Sec. 502(a) (2) of ERISA and seek to hold them liable for the full panoply of relief available under ERISA Sec. 409 in the event of a fiduciary breach.

Mertens in no way affects the relief available from a fiduciary under Sec. 409 in an action brought to enforce its provisions under Sec. 502(a) (2), a matter expressly acknowledged by the U.S. Supreme Court in the Mertens decision. Accordingly, Mertens does not jeopardize the relief available to the Department under the express provisions of the ERISA civil enforcement scheme designed to address fiduciary misconduct—ERISA Secs. 409 and 502(a) (2). Nor does it threaten the relief available to plan participants who likewise are empowered to bring suit under these provisions.

Thus, Mertens clearly leaves intact the principal enforcement tools needed for the Executive Life litigation. However, even in the unlikely event that the Department of Labor or a participant would forego Sec. 502(a) (2) and instead proceed solely under Sec. 502(a) (3) or the parallel provision setting forth the Department's cause of action—Sec. 502(a)(5),[1] the Department to date has not explained how the Mertens decision jeopardizes its Executive Life enforcement activities. Mertens did not alter or change existing law as to the scope of available remedies under Sec. 502(a) (3) or Sec. 502(a) (5). Just as before, these provisions expressly authorize injunctions and "other appropriate equitable relief" to "redress" violations of ERISA or "enforce" its terms.

These traditional equitable concepts should be more than adequate to ensure the availability of effective and adequate relief in the Executive Life context. For example, an injunction directed to a plan sponsor to provide a "back-up" or alternate annuity should remain available as a form of appropriate relief to redress a violation of the Act. Similarly, in situations where the claim focuses on an inappropriate reversion of plan assets to a plan sponsor, traditional equitable concepts such as "unjust enrichment" or the use of "constructive trusts" are available to protect the interests of participants. Moreover, given their broad powers to fashion appropriate equitable relief, the district courts undoubtedly will turn to other avenues to ensure that violations of ERISA do not go unreserved.

Because Mertens does not change the relief available under Sec. 502(a) (3) or (a) (5), we are unable to see why the equitable relief the statute expressly authorizes is inadequate or threatens the ongoing Executive Life litigation.

THE EXECUTIVE LIFE WORKOUT

The sense of crisis in the Executive Life litigation may have arisen from a misunderstanding of what pensioners have really lost. One statement heard over and over again in the Senate Labor Committee markup was that unless legislation was passed immediately to overturn Mertens, thousands and thousands of Executive Life annuitants would be left with nothing.

I am glad to correct that statement by reporting to you information supplied by the National Organization of Life and Health Guaranty Associations (NOLGHA). NOLGHA reports that under the current rehabilitation plan, 93 percent of the 86,400 participants for whom Executive Life annuities were purchased are expected

[1] Sec. 502(a)(3) authorizes action by plan fiduciaries, participants or beneficiaries for "appropriate equitable relief—to redress" violations of ERISA or "to enforce" the terms of ERISA or a plan. Sec. 502(a)(5) authorizes the Secretary to bring an action for the same relief.

to receive 100 percent of their monthly benefits. Indeed, they have been receiving 100 percent since April, 1992. In addition, the conservator arranged, in May of this year, for the approximately 30 percent shortfall from the first year of the conservatorship to be paid immediately out of funds contributed by the State guaranty associations.

The remaining 6,600 participants may receive less than 100 percent. Of those, approximately 4,200 may receive less because the value of their benefits exceeds their respective State guaranty association's statutory benefit limit, typically $100,000 although some states provide a $300,000 or higher benefit. Two thousand four hundred people may receive less because they live in states that did not have a guaranty association law at the time of the Executive Life failure. All three jurisdictions have since adopted guaranty systems to deal with possible future problems. Thus, with the State provided safety net, at worst, these participants will receive at least 77 percent of their monthly benefits. In addition, ERISA offers a complete recovery in those cases where a fiduciary breach may be proven.

In addition, under the workout, partially and uncovered participants in pay status who had their benefits cutback to 70 percent during the first year of the rehabilitation will receive a lump sum payment covering the 30 percent missed payment amounts plus interest.

I am sure representatives from NOLGHA would be happy to provide you with more details about the Executive Life workout if you are interested.

Of course, this is not to say that DOL should abandon its suits arising out of the financial failure of Executive Life. I mention the proposed workout to correct the perception that unless DOL gets retroactively effective legislation, Executive Life annuitants will get nothing.

In conclusion, as this Committee well knows, ERISA was enacted after 10 years of exhaustive and careful study including scores of hearings and extensive testimony. That fact alone illustrates that there are no quick, simple or easy answers to Federal regulation of the Nation's private pension system. Clearly, the linchpin of ERISA is the underlying belief that private employee benefit plans, voluntarily adopted and maintained by employers for the benefit of employees and their beneficiaries, are to be encouraged to provide retirement security for working Americans. Promoting these twin goals, protecting participants benefits while encouraging employers to adopt and maintain these voluntary plans, is the fine and delicate balance struck by Congress when it enacted ERISA. It should not be changed without clear and convincing evidence that such change is appropriate.

We are pleased to be with you today to work with you to maintain these goals. We would be happy to furnish you with any additional information or answer any questions you may have.

Senator METZENBAUM. Thank you very much, Mr. Klein.

Both of you State that your organizations disagree with the Department of Labor as to the remedies still available in light of the Mertens decision as it pertains to the Department's Executive Life litigation. I would like to ask both of you what remedies do you believe are still available, and on what case law do you base that view.

Mr. Vine, do you want to go first?

Mr. VINE. Sure. I think there are many remedies available. I assume you are asking the question in the context of remedies against nonfiduciaries, because the one thing that Mertens makes absolutely clear is that there are remedies against fiduciaries. ERISA is unequivocal in that respect, and the only issue that Mertens addressed related to recovery of damages from a nonfiduciary.

When you focus on nonfiduciaries, the question first is, Is the service provider in fact a fiduciary. ERISA includes a very broad definition of fiduciary, and makes available to plaintiffs a cause of action against anyone, whether or not he is formally designated as a fiduciary.

In addition, the Court made clear that traditional equitable remedies may be available against a service provider, that is, restitution or injunctive relief. In addition, a fiduciary who has a contract

with a nonfiduciary service provider, or who has a claim against the nonfiduciary for other reasons, malpractice, for example, might bring an action against him, and if a court felt that the fiduciary wasn't doing his job in pursuing any claims he had against the nonfiduciary, a court could order him to pursue those claims.

Senator METZENBAUM. Mr. Klein, do you agree?

Mr. KLEIN. Senator, I thought perhaps your question might have been referring to the issue of the availability of the purchase of backup annuities as a form of relief. Our view would be that the law is already clear that the purchase of a backup annuity is equitable relief, which is therefore an available remedy.

Senator METZENBAUM. Mr. Vine, you indicated that the only remedies would be available against nonfiduciaries. What about the remedies available against fiduciaries?

Mr. VINE. I had intended to make clear in the first part of my answer that ERISA makes it absolutely clear that plaintiffs have claims directly against the fiduciary. My point was only this, that Mertens did not involve a claim against a fiduciary. So I believe that ERISA provides a broad array of remedies against the fiduciary itself.

Senator METZENBAUM. Executive Life failed in April of 1991. Retiree annuities were reduced by 30 percent for 1 year. To the extent that pension plans purchased those annuities in violation of ERISA, I would ask both of you, shouldn't those retirees have a right to receive 100 percent of their promised benefits, and on a timely basis?

Mr. VINE. ERIC's position is that retirees should receive every penny that they are entitled to under their plan. It is extremely regrettable whenever there is either a failure to receive pensions that are due, or a delay, as the Senator points out. It is our hope that in the Executive Life situation, the retirees will receive just that.

Many retirees are receiving and will receive full payment; we think it is going to be the vast majority of them that will receive their full payment, or virtually full payment, through the rehabilitation plan. In addition, many employers have come to the Department of Labor seeking relief so that they could provide supplemental payments to their plans. And in addition, in some cases where there has been a breach of fiduciary responsibility, we hope that the plaintiffs will be able to recover what is due them.

Senator METZENBAUM. Mr. Klein, do you care to comment?

Mr. KLEIN. I would concur with Mr. Vine's recitation of it and again point to the comments in my prepared statement about the information that 93 percent would already appear to be getting 100 percent. Even Mr. Miller indicates that for the moment he has been getting 100 percent. But clearly, where there may be annuitants who are not getting it, that's a real problem, and I think perhaps that is the narrow type of problem that your legislation today is aiming to focus at.

Senator METZENBAUM. Both of you note in your testimony that approximately 7,000 of the Executive Life annuity holders are unlikely to receive 100 percent of their retirement benefits. Is there any reason that these retirees, who never chose Executive Life, should lose a penny of their retirement income, and if they shouldn't, who should be responsible?

Mr. VINE. Well, first, as I mentioned, if a retiree is entitled to a pension of a given amount, he ought to receive the full amount. As to who should be responsible if he doesn't, that is going to depend on the particular facts of the case. In many cases, fiduciaries acted perfectly responsibly in selecting a particular annuity carrier, and as things turned out, the insurance company was not as financially strong as the fiduciaries reasonably believed at the time. In a case like that, I would not hold the fiduciaries responsible for being the backup insurer to an insurance company that, for reasons that could not have been and weren't anticipated, encountered financial difficulties.

On the other hand, in those cases where there was mismanagement or abuse or breach of fiduciary responsibility, the fiduciary should be responsible.

Mr. KLEIN. I want you to know, Senator, that in no way, shape or form do I come here to carry any brief for the Executive Life Insurance Company. I have a number of members of my association who are responsible insurance companies; those companies have lost twice because of the actions of Executive Life. First, they didn't get the business because Executive Life beat them out for it, and now they are left to clean up the mess because they are ultimately the guarantors behind the State guaranty associations.

So I would not want in any way, shape or form for our comments to be construed as standing up for Executive Life.

Senator METZENBAUM. Well, let me ask you this. What about the responsibility of the acquiring company—Mr. Hurwitz in this instance and his company, Pacific Lumber. Where there is a preconceived plan to go in and terminate the pension plan—I remember 1 day we were having a hearing here, and we learned that Mr. Ron Perlman was taking over Coleman Lantern, again in a leveraged buyout, and again with the money coming from Executive Life to buy some of the bonds. And we on this committee started jumping up and down about it, and in the middle of the night they changed signals and didn't go forward with the choice of Executive Life. Fortunately, for the Coleman Lantern employees, they were not put into that situation.

But my concern is that these leveraged buyout operators sometimes wind up in the position of being the fiduciaries, and sometimes they don't, but it is all part of a premeditated, prearranged plan, to move in, take over a company, terminate the pension plan—we have pretty much put a stop to that now by reason of some other legislation that I have been involved with that you are aware of.

But if we look backward, shouldn't the actual perpetrators of the whole game plan, the corporation that was putting the deal together in this manner, whether it was the Ron Perlmans or the Henry Kravitzes or the Hurwitzes, or whomever, were those who were manipulating the leveraged buyout, shouldn't they accept the total responsibility, because most often, they are the ones who name the new fiduciaries?

Mr. KLEIN. I would like to respond to that in two ways, first of all, to point out that notwithstanding the comment I made just a moment ago about Executive Life, that it does need to be said that at the time many companies bought Executive Life annuities, it

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was a very highly rated company, in fact, had the top rating. So I don't think it therefore follows that there was any kind of fiduciary breach per se on the part of a company that in fact went out and bought a company that had this tremendous rating.

But more specifically in answer to your last question, the Court has found that in those cases that they are fiduciaries, so they may very well, if a fiduciary breach can be found, have that liability.

I think the real issue that you and I both care about and have a mutual interest in is ultimately that the participants are taken care of, and I think that through the equitable remedies that are now available, but which may be clarified by S. 1312, we can help ensure that.

Senator METZENBAUM. Mr. Vine, did you care to respond?

Mr. VINE. Thank you, Senator, I would.

I think it would be presumptuous of me to comment on any particular case until I knew all the facts. But I think to the extent that your question suggests that if there are people in effect who are really pulling the strings in a particular arrangement who, although lurking behind the scenes, are really controlling the plan and controlling the decision to purchase annuities from a particular carrier, and doing so in a way that is not consistent with ERISA's fiduciary responsibility standards, I think those individuals would be fiduciaries under ERISA because of its very broad definition. The fact that they are not formally named in the plan as fiduciaries doesn't protect them. And under existing law, there are ample remedies against such persons.

Thank you.

Senator METZENBAUM. Thank you.

Mr. Klein, you make the statement———

Mr. SIGMAN. Mr. Chairman, may I respond very briefly to a point that Mr. Vine made—I am sure, perhaps, inadvertently. He sounded to me a little bit like an overly optimistic plaintiff's lawyer, and I am sure he did not intend to do that.

But the problem that we are faced with—we faced it in the Mertens case, and we are facing it here—is that the plan has been terminated. When Mr. Vine says that restitution is a remedy that would make plan participants whole, he is simply misstating the case. The plan has been terminated. It is not all that clear that a plan participant can achieve a remedy which would make him or her whole, because if the plan has been terminated, there are Federal courts out there which, under the direction of the U.S. Supreme Court now, are applying an extremely narrow and literal approach to this statute and take the position that, well, there is no plan; how can you therefore make this plan whole? How can you restore losses to the plan if the plan has been terminated? And that is another variation of the Catch-22 situation that my client Mr. Miller finds himself in.

In addition, it is not all that clear that plan participants and retirees in this country have a malpractice action any longer. We haven't had the opportunity today to address the issue of ERISA preemption, but ERISA preemption has had a devastating effect on retirees and plan participants who are seeking redress.

We survived the preemption motion in the Hewitt case against Hewitt; that was before the U.S. Supreme Court. But the dicta in

that opinion, as the dissent points out, a dissent joined in by Chief Justice Rehnquist, really raises doubt now as to whether or not there is any cause of action whatsoever under Federal or State law against a nonfiduciary who aids and abets a fiduciary in the commission of a breach. And it also raises questions as to whether or not any State claim, such as a traditional malpractice claim, has survived.

Senator METZENBAUM. Thank you, Mr. Sigman.

Mr. VINE. If I may, I would just like to respond briefly, with the Senator's permission.

Senator METZENBAUM. Surely.

Mr. VINE. First, as to the absence of any remedy because the plan doesn't exist, I think the Federal courts clearly do have the authority to be creative and to award remedies, and in the 9th Circuit, there is an outstanding case, the Amalgamated Clothing and Textile Workers Union case, which provides that in extraordinary circumstances, the courts will provide relief where no other relief would be available.

As to malpractice actions, in the Mertens case, there is an outstanding malpractice claim being brought, and I am not aware of any case that makes it clear that that is not a good claim if the facts warrant it. And of course, I pass no judgment on whether the facts support it, but I think the remedies are there where malpractice does occur.

Senator METZENBAUM. Let me finish up with one question to you, Mr. Klein. You make the statement that overall, the State guaranty funds and ERISA have worked well in the Executive Life case. I have difficulty in believing that any one of the 84,000 affected workers and retirees would agree with you.

Isn't it true that prior to ERISA, trust law provided monetary damages to individuals as an equitable relief?

Mr. KLEIN. The reason I think many of the 86,400 participants would agree with me is that it appears that at least 93 percent of them are getting 100 percent of their benefits; those who are not are getting at least 77 percent of their benefits, and as a result of either further resolution of the estate of Executive Life, or other pending litigation that may benefit the estate of Executive Life, and ERISA actions that may prove a fiduciary breach may mean that they will get 100 percent.

But we have come here to tell you that to the extent that they do not, that is a real problem that we think you are to be commended for helping address.

Senator METZENBAUM. As a matter of fact, isn't it true that prior to ERISA, nonfiduciaries who knowingly participate in a violation of trust law were liable for their actions, and that what we have done with ERISA is we have changed that somewhat, or rather, the courts have interpreted it to indicate that we have changed it; I don't think we intended to so change it.

Mr. KLEIN. I'll let Ted Rhodes answer that.

Mr. RHODES. Thank you.

In terms of ERISA, it is a little bit different than the common law in the sense that ERISA drafted a very broad definition of fiduciary. There is also a definition of "parties and interests" under ERISA, which has a number of listed prohibitions in terms of

transactions, and actions can be brought to enforce recovery under those prohibited transactions under all the provisions of the 502(a)(3) relief provisions of ERISA as well.

Senator METZENBAUM. I gather you two are lawyers, and you are not, Mr. Klein?

Mr. KLEIN. I am a lawyer; I am just not as expert as my general counsel.

Senator METZENBAUM. All right. We ought to let them earn their keep, so I will ask them both a question. Why should workers and retirees have less legal protection under ERISA than they had prior to ERISA? Doesn't that give you some cause for concern?

ERISA was enacted to protect the funds, to protect the employees; doesn't it bother you that under ERISA, the courts have now gotten to the point where the fiduciary obligations are not as great as they were prior to the enactment of statutory legislation?

Mr. RHODES. We would tend to say that ERISA was enacted with a true balance in mind between the maintenance of a voluntary system and the protection of participants and beneficiaries. We have seen that voluntary system expand in terms of coverage and dollars that are provided to employees, and our concern is the concern that was expressed on the House side when our witness testified from U.S. West, that for employers who are maintaining plans when they are providing significant benefits, litigation that arises in those situations—like, for example, they have 140 claims a month that they are processing, and the individual witness was the manager of those claims and reviewed those for legal actions—out of 4,000 claims in a 2-year period, there were 17 lawsuits, and they successfully defended against all 17 lawsuits, and their legal fees have been $3 million. So from their point of view, the balance necessary to maintain that plan and ensure the benefits of participants and beneficiaries has to be weighed in that whole process. We are clearly worried about participants and beneficiaries getting their benefits, but we are worried about those plans continuing to be maintained, too.

Senator METZENBAUM. Mr. Vine.

Mr. VINE. As the Senator pointed out, ERISA is a remedial statute, but as I commented earlier, it is more than a remedial statute. It is also designed to encourage employers to adopt and maintain benefit plans for their employees. These plans are, after all, voluntary, and what the framers of ERISA sought to do, and as Mr. Rhodes pointed out, was to strike a balance here so that employers would not be discouraged by the costs of excessive liability from continuing to provide benefits to their employees.

Senator METZENBAUM. Thank you very much.

I want to thank all the members of the panel. We appreciate your cooperation, and we hope to move this legislation very promptly.

The hearing stands adjourned.

[Whereupon, at 11:38 a.m., the subcommittee was adjourned.]

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