



Statement on
Joint Trusteeship of Pension Plans and its Impact on Market
Performance: An Analysis of EBRI Data
Hearings on Joint Trusteeship of Pension Plans
Before the U.S. House Education and Labor Subcommittee on
Labor Management Relations

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by

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An Analysis of EBRI Data**

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Summary

- Due to differences in asset allocation, jointly trusteeed plans achieved a five-year annualized rate of return 2.6 percentage points below non-jointly trusteeed defined benefit funds
- If non-jointly trusteeed defined benefit funds had achieved this lower rate of return, they would have had to contribute an additional \$87 billion to end the period with the same total assets
- These data show a significant difference in asset allocation and return by plan type and trustee form, yet this cannot be used definitively to settle the debate on joint trusteeship
- Asset allocation for the \$764 billion in single-employer defined benefit plans is 40.3 percent in equity, 16.4 percent in bonds, 4.1 percent in cash, and 39.2 percent in other assets
- For the \$466 billion in single-employer defined contribution plans, the asset allocation is 44.2 percent in equity, 7.1 percent in bonds, 13.5 percent in cash, and 35.2 percent in other assets
- The \$146 billion in multiemployer plans is allocated with 29.2 percent in equity, 38.7 percent in bonds, 8.5 percent in cash, and 23.6 percent in other assets
- The total assets of single-employer defined benefit plans enjoyed a 7.4 percent rate of return for the third quarter of 1989, a 22.9 percent one-year return, and an annualized five-year return of 18.1 percent, all periods ending with the third quarter of 1989
- Single-employer defined contribution total assets experienced a 9.7 percent quarterly return, a 24.6 percent one-year return, and an annualized five-year return of 17.3 percent, all periods ending with the third quarter of 1989
- Total assets of multiemployer plans experienced a 5.3 percent quarterly return, a 18.9 percent one-year return, and a 15.5 percent annualized five-year return, all periods ending with the third quarter of 1989

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Introduction and Overview

Legislation that would require that the assets of a private, single-employer pension plan be held in trust by a joint board of trustees consisting of an equal number of employers and participants has sparked an intense debate among employers, workers, and policymakers. The bill (H.R. 2664), introduced on June 15, 1989, by Rep. Peter Visclosky (D-IN), is expected to gain increased attention as Congress focuses on the perceived short-term investments of pension funds. Especially critical will be emphasis on the comparison of single-employer plans and multiemployer plans because multiemployer plans have had equal union and employer representation on investment boards mandated by law, primarily by the Labor Management Relations Act (Taft-Hartley Act) in 1947.

EBRI's *Quarterly Pension Investment Report (QPIR)* contains data pertinent to this bill by presenting the asset allocation of single-employer defined benefit plans, single-employer defined contribution plans, and multiemployer plans. There are also data on the income and contribution flows and rates of return for these plans. In *QPIR*, single-employer plans include plans that are and are not collectively bargained. Multiemployer plans include Taft-Hartley plans.

The Taft-Hartley Act of 1947 applies to union administered employee benefit plans. Therefore, only these multiemployer plans are required to have joint representation on the board of trustees. Most multiemployer plans are of this type. There are single-employer plans which are bargained with a union, but employers generally retain significant control over all aspects of the plan. Therefore, this bill

would principally affect single-employer plans and multiple employer plans. Comparisons with multiemployer plans include decisions on investment managers, asset allocation, and may include specific investments as well as comparisons of the return on the investments.

Equity rates of return are similar for single-employer plans and multiemployer plans. Overall, multiemployer plans have lower rates of return for all assets probably due to the different allocation. These data show that the asset allocation of multiemployer plans differs from that of either single-employer defined benefit or single-employer defined contribution plans with multiemployer plans more heavily invested in bonds. Since bonds have historically had lower rates of return, the asset allocation difference may be the major reason for the difference in overall rates of return. For the five years ended with third quarter 1989, the Shearson-Lehman-Hutton bond index showed an annualized five-year return of 13.2 percent compared to an annualized five-year return of 20.3 percent for the Standard & Poor's 500 (a commonly used index for equity investments). The reasons why multiemployer plans invest a larger proportion of asset in bonds is investigated later in this paper.

Single-employer plans and multiemployer plans, however, do not operate in perfectly comparable environments. While all these plans are governed by the Employee Retirement Income Security Act of 1974 (ERISA), all multiemployer plans must also relate to the contracts negotiated with the union while not all single-employer plans are negotiated. Other factors may also limit the comparability of these numbers including workforce age and tenure, investment objectives, and the need or desire for stable contributions among others.

This paper presents the EBRI data and draws general conclusions. Also, the differences between the environments of single-employer and multiemployer plans

are presented so that an evaluative eye can view the data and make an individual judgement about the effects of joint trusteeship on pension plan investments.

Data Source and Organization of Data

QPIR results from a joint project with the Department of Labor (DOL), the Federal Reserve Board and EBRI. This same data base is used to generate the Federal Reserve Board Flow of Funds numbers for pension assets as well as pension numbers for the Income and Product Accounts for the Department of Commerce. Data from DOL Form 5500, which all pension plans must file, are used for the years that these data are available. To project beyond this, EBRI and the Federal Reserve Board use data from Wilshire Associates and SEI to project these data to estimate the current level of assets.

The data are available for private trusted pension plans. These plans are then divided by single-employer and multiemployer plans. The single-employer plans are divided by defined benefit and defined contribution. Multiemployer plans are not divided by plan type, but DOL states in 1985 that nearly 75 percent of multiemployer plans were defined benefit. For the purposes of this paper, the single-employer defined benefit plans, the single-employer defined contribution plans, and the multiemployer plans will constitute the plan types.

Data

Asset Allocation — The asset allocation of the \$764 billion in single-employer defined benefit plans is 40.3 percent to equity, 16.4 percent to bonds, 4.1 percent to cash, and 39.2 percent to other asset categories. This compares to the asset allocation of the \$466 billion in single-employer defined contribution plans with 44.2 percent in equity, 7.1 percent in bonds, 13.5 percent in cash and 35.2 percent in other assets. Finally, the \$146 billion in multiemployer plans is allocated with 29.2 percent in

equity, 38.7 percent in bonds, 8.5 percent in cash and 23.6 percent in other assets (chart 1). Therefore, a notable difference does exist in asset allocation by plan type.

Flows — The flows of the different types of private pension funds also denote similar differences. All plan types experienced net withdrawals overall and experienced large capital gains relative to those net withdrawals.

In 1988, defined benefit plans experienced net withdrawals of \$18 billion. Of that, most of the withdrawals came from equities. Counteracting these net withdrawals, defined benefit plans received \$38 billion in dividends and interest and experienced \$55 billion in capital gains during 1988. Flows, then, for defined benefit plans totalled a \$75 billion inflow largely from capital gains (table 1).

Defined contribution plans also had net withdrawals during 1988 of \$16 billion, again mainly from equities. These plans received dividends and interest of \$23 billion and experienced capital gains of \$32 billion. For defined contribution plans, flows totalled an inflow of \$39 billion.

Flows for multiemployer plans totalled \$13 billion during 1988. Net withdrawals totalling \$2 billion came largely from bonds. These funds received \$9 billion in dividends and interest and nearly \$6 billion in capital gains.

Rates of Return — The rates of return also varied by plan type. Defined benefit plans experienced a 7.4 percent return on all assets during the third quarter of 1989, a one year return ending September 30, 1989, of 22.9 percent, and an annualized five year return ending September 30, 1989, of 18.1 percent. The equity investments of these plans achieved a rate of return for the third quarter of 11.0 percent, a one year return of 33.6 percent, and a five year annualized return of 22.5 percent (again, all periods ending on September 30, 1989). Finally, bond investments by defined benefit plans achieved a 0.8 percent quarterly return, a 11.8 percent one year return, and a 12.6 percent five year return (table 2).

Defined contribution plans experienced a higher quarterly rate of return for total assets though slightly lower returns for the longer time periods. Equity investments of these funds achieved rates of return which were equal to or higher than those achieved by the single-employer defined benefit plans. Bonds had higher returns for all time periods.

Total assets of multiemployer plans experienced rates of return which were consistently lower than either type of single-employer plan. Equity investments, however, outperformed the other plan types for all time periods except for the quarterly return. Finally, bond investments achieved comparable returns to the other plan types.

What the Data Show

QPIR emphasizes the effects of asset allocation. A much larger proportion of market experience (including dividends, interest, and capital gains) for single-employer defined benefit plans is derived from the stock market, while bonds account for the bulk of multiemployer plans income. This is a direct result of the different asset allocations. In addition, as can be seen from table 2, the returns on equity and bonds do not vary dramatically between plan types in the 1, 3, or 5-year returns. The overall returns, however, do vary with multiemployer plans' returns and are lower than the returns for single-employer defined benefit and defined contribution plans. Since the bond rates of return are lower than the equity rates of return and the multiemployer plans have a larger share of assets invested in bonds, the overall return is largely a result of the different asset allocation by plan type.

Notably, the defined contribution plans also lag the defined benefit plans overall returns while outpacing the equity returns for defined benefit plans. The asset allocation of defined contribution plans are most similar to defined benefit plans although a higher investment in cash may account for some of this difference.

These data again emphasize the effects of asset allocation, although the Visclosky bill would presumably not affect those plans in which participants already control most of the investment decisions.

What Causes the Difference?

Why are there differences in the asset allocation and flows between single-employer defined benefit plans and multiemployer plans? This question is central to the debate. If the difference was entirely due to the required joint trusteeship in multiemployer plans then one could assume that had single-employer plans also been required to have joint trusteeship their asset allocation would have been the same as multiemployer plans. EBRI estimates from *QPIR* data that with this asset allocation single-employer plans would have had to make an additional \$87 billion in net contributions from the end of 1982 through third quarter 1989 to achieve the same asset level they currently have.

Several other factors beyond joint trusteeship may also come into play. Because *QPIR* does not allow for the breakout of these effects, this section will provide an overview of some of the possible influences.

Multiemployer plans operate in a different environment than single-employer plans since all multiemployer plans negotiate with unions and agree on contributions as part of the negotiations. The contribution rates are frequently set for a 3 to 5 year term. In this way the multiemployer trust fund, to which all contributions are made, can estimate future contributions it will receive and participating employers can estimate all future contributions.

Single-employer plans can change their contributions at any time with the approval of the named fiduciary and within the minimum and maximum contributions allowed by law. These limits were drawn closer together with the Omnibus Budget Reconciliation Act of 1987.

Edward Callan, chairman of Callan Associates, notes that if single-employer plans experience a decline in their equity performance, the corporation simply makes larger contributions to compensate. If a multiemployer fund experiences losses on equity investments, then the plan must go back to the bargaining table and negotiate larger contributions.¹

Another variable which has been mentioned as a difference in the investment of multiemployer and single-employer plans is the age and tenure of the participants. The argument states that multiemployer plans have, on average, older employees with longer tenure which prompts the board of trustees to invest in bonds to preserve investment performance of the past, preserving the monies for the benefits that will need to be paid in the near future. Single-employer plans with an overall younger workforce could invest more in equities which over many years would even out fluctuations in the market. There is no consensus that these workforce differences do, in fact, lead directly to the different asset allocation.

Motivations have also been discussed as a reason for the differences. Perhaps, the argument goes, multiemployer plans with employee representation on the board of trustees, make more long-term investment decisions and do not try to outsmart the market through many trades which could feed the volatility of the stock market purported to be created by other institutional investors. Evidence for this argument are sparse and largely anecdotal. EBRI is currently beginning a study of turnover rates and investment time horizon for defined benefit and defined contribution plans in both single-employer and multiemployer plans.

Finally, the issue of social investing has occasionally been mentioned in this arena. Would increased employee representation encourage more social investing and would this be advantageous for society as well as the participants and

¹Phyllis Feinberg. "Taft-Hartley Plans Remain Conservative with Investments," *Pension World*, November 1988, pp. 32-36.

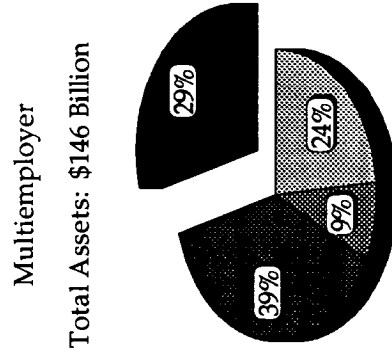
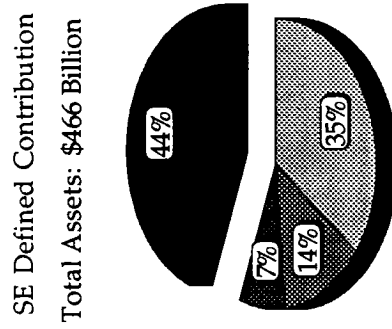
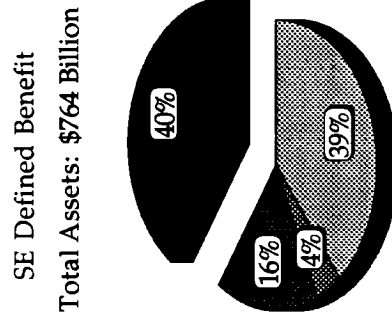
beneficiaries of the plan? Some feel that increased social investing is highly desirable in all pension plan investing; others feel that an overemphasis on social investing will detract from return and perhaps increase risk, each of which would be detrimental to the plan sponsor in terms of larger contributions and to the employees in terms of fewer or lower benefit increases.

How Others Have Used the Data

QPIR data has been used by many participants in this debate. The data do clearly show that single-employer plans would be more expensive for employers and, in the short term, the Federal Treasury were joint trusteeship to lead to a change in asset allocation to that of jointly trustee multiemployer plans. The data in *QPIR* cannot, however, be used definitively to settle the debate over this proposal for three reasons: (1) the data does not allow the user to split out different reasons for asset allocation or the motivations behind the decisions; (2) even if the motivations were split, there is debate on which would be the most advantageous for society, in addition to the participants and beneficiaries; and (3) the Congress might view the public policy reasons for change as overriding any economic costs.

The future project of EBRI concerning turnover and investment decision motivations will shed some light in this area. Preliminary results will be available this summer.

Chart 1
Asset Allocation for September 30, 1989, by Plan Type



Equity
 Bonds
 Cash
 Other

Table 1
Net Flows for 1988, by Plan Type

Flows	Single Employer Defined Benefit	Single Employer Defined Contribution (billions)	Multiemployer
Earnings			
Dividends and Interest	\$37.6	\$22.7	\$9.2
Capital Gains	55.4	31.9	5.5
Net Contributions			
Equity	-12.0	-18.8	-1.6
Bonds	-7.6	-1.9	-3.6
Cash	-0.9	9.3	3.8
Other Assets	2.7	-4.1	-0.8
Total Net Contributions	-17.8	-15.5	-2.2
Total Net Flows	\$75.2	\$39.1	\$12.5

Source: EBRI *Quarterly Pension Investment Report*, third quarter 1989.

Table 2
Rates of Return, Ending September 30, 1989

Plan Type and Indices	Period			
	Quarter 89Q3	1 Year 88Q4-89Q3	3 Year ^a 86Q4-89Q3	5 Year ^a 84Q4-89Q3
All Assets				
Single Employer DB Plans	7.4%	22.9%	16.5%	18.1%
Single Employer DC Plans	9.7%	24.6%	15.8%	17.3%
All Multiemployer Plans	5.3%	18.9%	12.4%	15.5%
Consumer Price Index	0.7%	4.3%	4.3%	3.4%
Equity				
Single Employer DB Plans	11.0%	33.6%	20.9%	22.5%
Single Employer DC Plans	12.3%	33.9%	20.9%	23.3%
All Multiemployer Plans	11.6%	34.1%	21.3%	22.5%
S&P 500	10.7%	32.9%	18.6%	20.3%
Bonds				
Single Employer DB Plans	0.8%	11.8%	8.7%	12.6%
Single Employer DC Plans	1.8%	17.5%	10.5%	13.7%
All Multiemployer Plans	0.9%	12.2%	8.8%	14.0%
Shearson/Lehman ^b	0.9%	11.3%	8.1%	13.2

Source: EBRI *Quarterly Pension Investment Report*, third quarter 1989, revised.

^aThree- and five-year returns are expressed as annualized rates.

^bShearson Lehman Brothers Kuhn Loeb Government/Corporate Bond Index.