Testimony of Scott Henderson, Treasurer and Vice President for The Kroger Co.

On "Assessing the Challenges Facing Multiemployer Pension Plans"

U.S. House Education and the Workforce Committee,

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Thank you Chairman Roe, Ranking Member Andrews, and members of the Subcommittee for the opportunity to testify today. My name is Scott Henderson. I am the Vice President and Treasurer for The Kroger Co. ("Kroger"). I have responsibility for Kroger's pension investments, and I serve as a Trustee for one of the 33 multiemployer pension plans in which Kroger participates.

I. ABOUT THE KROGER CO.

Kroger is one of the largest retailers in the world, operating 2,425 supermarkets, 789 convenience stores, 337 fine jewelry stores and 37 food processing facilities. We have operations in more than 35 states and sales of more than $90 billion. Kroger's net earnings margin is just over 1%, reflecting the highly competitive nature of the retail food industry.

Kroger ranks 23rd on the list of Fortune 100 companies and has been recognized by Forbes as the most generous company in America. We support numerous charities and more than 30,000 schools and grassroots organizations in the communities it serves. Kroger contributes food and funds equal to 160 million meals each year through more than 80 Feeding America food bank partners.

Kroger employs 339,000 associates. Approximately two-thirds of our associates are covered by roughly 300 collective bargaining agreements ("CBAs"), making Kroger one of the largest unionized employers in the United States. Kroger's primary union is the United Food and Commercial Workers International Union ("UFCW"), which represents almost 96% of our unionized workforce. Kroger's other unions include the Bakery, Confectionary, Tobacco, Grain Millers International Union ("BCTGM"), the International Brotherhood of Teamsters ("IBT"), the International Union of Operating Engineers ("IUOE"), the International Association of Machinists ("IAM"), the Service Employees International Union ("SEIU"), the United Steel, Paper and Forestry, Rubber, Manufacturing, Energy, Allied Industrial and Service Workers International Union ("USW"), and the National Conference of Fireman & Oilers ("NCFO").

Kroger contributes to 33 multiemployer defined benefit pension plans. In 10 of these plans, we account for 5% or more of the plan's total contributions. On average, Kroger contributes approximately $250 million per year to these plans. However, as described in greater detail below, Kroger could be required to contribute an additional $2.3 billion over the long-term (in addition to its contributions to cover current accruals) to fund pension benefits previously accrued under these plans.

II. WHAT IS A MULTIEMPLOYER DEFINED BENEFIT PENSION PLAN?

A. General Overview

A multiemployer defined benefit pension plan is a retirement plan to which more than one employer contributes. These plans are jointly managed by a board of trustees and funded pursuant to a CBA. Multiemployer plans were designed to serve as retirement vehicles for smaller employers and employers with mobile workforces, where employment patterns prevented employees from accruing adequate retirement benefits under traditional defined

benefit pension plan sponsored by a single company. In other words, multiemployer plans were established so that workers' pensions could be portable as they moved from job-to-job within the same industry.

Multiemployer plans are subject to the Labor Management Relations Act of 1947, otherwise known as the Taft-Hartley Act. These plans are also subject to the Employee Retirement Income Security Act of 1974 ("ERISA") and the relevant provisions of the Internal Revenue Code of 1986. These plans are required to have equal employer and union representation on the governing board of trustees. In general, the bargaining parties (i.e., the employer and the union) negotiate the terms under which employer sponsors contribute to the multiemployer plan. The board of trustees determines the benefits to be provided by the plan, based on the level of plan contributions and actuarial assumptions. Although the trustees are selected by management and labor, they are required by law to act solely in the interests of plan participants.

B. Withdrawal Liability

Prior to the enactment of ERISA and the Multiemployer Pension Plan Amendments Act ("MPPAA"), an employer's obligation to a multiemployer plan was generally limited to the contribution obligation established in its CBA. In other words, a contributing employer's exposure to these plans was limited to the contribution it was required to make during the term of the CBA. Once it made the agreed-upon contribution, the employer had no further liability. Thus, if it terminated participation in a multiemployer plan following the expiration of its CBA, it did not have any further liability to the plan.

In 1980, Congress enacted MPPAA. MPPAA was designed to address perceived problems with the multiemployer pension plan rules, including the possibility that an employer could terminate participation in a plan without having fully funded its share of plan benefits. MPPAA, in turn, strengthened the manner in which pension benefits were protected by requiring contributing employers that terminated their participation in a plan to make payments to cover their share of any unfunded benefits. This is known as "withdrawal liability."

C. "Last-Man Standing" Rule

When a withdrawing employer fails to pay its portion of the plan's unfunded liabilities – as is commonly the case with employers that become bankrupt or simply go out of business – responsibility for funding these unfunded liabilities is shifted to the remaining contributing employers. This is referred to as the "last-man standing" rule.

Even in those cases where an employer exits a plan and fully pays its withdrawal liability, the remaining employers are still responsible for ensuring that there is adequate funding in the future to cover plan liabilities attributable to the exiting employer. Thus, if the plan has adverse investment experience, the remaining employers must ultimately fund the benefits of the workers and retirees of the withdrawn employer. For example, assume an employer leaves a plan and pays $100 million in withdrawal liability (representing 100% of the amount it owes) but the plan suffers a 25% investment loss in the following year (as many plans did in 2008). Unless the plan experiences future "excess" investment returns that make up the loss, the "last-man standing" rule requires the remaining employers to make up the $25 million shortfall. In other words, the remaining employers bear the investment (and mortality) risk for benefits attributable to the workers and retirees of the employer that exited the plan (notwithstanding the fact that the employer paid its withdrawal liability).

D. Implications of Withdrawal Liability and the "Last-Man Standing" Rule

It is important to emphasize that the "last man standing" rule effectively saddles employers that remain in a multiemployer plan with potential liability for pension obligations of workers and retirees that never worked for the remaining employers, worked for a competitor of the employers, or who worked in a completely different industry than the employers. This shifting of risk to the remaining employers places an unfair burden on these employers, and depending on their financial condition, could threaten the continued viability of these companies.

Not surprisingly, the "last-man standing" rule has effectively discouraged the entry of new employers into these plans. New employers do not want to join a multiemployer plan that could expose them to future withdrawal liability on benefits earned by employees of other employers, including benefits earned long before the new employer joined the plan.

E. Multiemployer Plans and the Pension Benefit Guaranty Corporation

Unlike single-employer defined benefit plans, the remaining employers in a multiemployer plan effectively guarantee plan benefits and the Pension Benefit Guaranty Corporation ("PBGC") plays a secondary role. Thus, unlike troubled single-employer defined benefit pension plans – where the PBGC receives the plan's assets, assumes the pension liabilities, and pays out benefits in the case of a distressed plan – in the case of a multiemployer plan, the PBGC loans money to the plan to pay benefits when the plan becomes insolvent. If this occurs, the pension payments must be reduced to the extent they exceed the PBGC statutory maximum. Currently, the maximum PBGC multiemployer guarantee is $12,870 per year for a retiree with 30 years of service at normal retirement age.

III. KROGER'S PARTICIPATION IN MULTIEMPLOYER DEFINED BENEFIT PLANS

Like many retail food employers, Kroger began participating in multiemployer plans in the 1960s – in an era during which its exposure to these plans was limited to the contribution it was required to make during the term of its CBAs. Thus, its decision to participate in these plans was made well before the transformational changes made by ERISA and MPPAA.

Employers in the retail food industry operate distribution centers and food processing facilities and transport goods between these facilities and store locations. As a result of its transit operations, Kroger, like a number of food employers, became contributing employers to trucking industry multiemployer plans during the 1960s – at a time when trucking companies dominated participation in these plans. As a result of the dramatic consolidation in the trucking industry since the 1980s, some of these plans have ceased to be trucking plans, and food and beverage employers – like Kroger – now represent the majority of contributing employers.

The effects of the market consolidation in the retail food and trucking industry was keenly felt when the 2001 tech bubble burst. The combined effect of the market consolidation and those losses were exacerbated by the 2008 stock market crash. These market events, together with the dramatic consolidation that has occurred in the trucking and food industries and the structural problems inherent in the multiemployer rules that have discouraged new entrants into the plans, have led to the current funding concerns.

As described in our annual report, Kroger could be required to make future contributions of an additional $2.3 billion (in addition to its contributions to cover current accruals) to fund previously accrued pension benefits under the multiemployer plans in which it participates. Approximately 70% of this exposure is attributable to five of these

plans. Importantly, a large portion of the $2.3 billion that Kroger could have to contribute is attributable to workers and retirees who never worked for Kroger.

IV. KROGER AS AN INDUSTRY LEADER

A. Kroger's Proactive Actions to Address Underfunding

Kroger has been innovative and forward-thinking in its approach to multiemployer pension funding issues. For example, in response to funding concerns, union and Kroger trustees have worked together to address the funding of the 11 multiemployer plans with a Kroger trustee through a combination of contribution increases and benefit adjustments. In addition, Kroger is a long-time proponent of multiemployer funding reform including increased transparency. Since 2005, Kroger has made disclosures in its Annual Report with respect to its participation in multiemployer plans, including the theoretical estimate of its aggregated exposure to the underfunding in such multiemployer plans. Kroger supported the efforts of the Financial Accounting Standards Board for greater financial statement disclosure of multiemployer plan exposure.

In 2011, Kroger acted to address underfunding of four UFCW multiemployer plans, in which it was effectively the "last man standing," by negotiating the merger of these four plans into one, new plan. In this case, Kroger associates accounted for over 90% of the active participants in these plans (which covered almost 30% of Kroger's represented workforce). Together, the four plans had a current market value funded ratio of about 73% and over $900 million of unfunded liabilities, *about $200 million of which was attributable to workers and retirees who had never worked for Kroger* (i.e., amounts that were shifted to Kroger on account of the "last-man standing" rule).

As part of the merger, Kroger agreed to accelerate its share of funding to the plan and fund the liabilities attributable to workers and retirees of employers that previously exited the plans. Kroger also made a long-term commitment (until 2021) to a defined benefit plan that is designed to provide competitive retirement benefits for career Kroger associates covered by the new consolidated plan. In January, 2012, Kroger contributed $650 million to facilitate the merger of the four plans and to eliminate most of the current underfunding. As a result of this contribution, the new consolidated plan's current market value funded ratio rose from approximately 73% to 91%.

B. Structural Impediments Prevent Faster Funding of Underfunded Plans

Notwithstanding these efforts, Kroger still faces significant exposure from underfunded plans, as do hundreds of other employers. The current funding structure of multiemployer plans discourages companies like Kroger from addressing those plans in which Kroger is not the dominant contributing employer. This is because the current funding rules effectively prevent employers like Kroger from eliminating their share of plan underfunding, unless the other contributing employers can be persuaded to take similar action (or the plan attempts to address the issue through special withdrawal liability rules and contribution agreements).

For example, the actions Kroger took last year to address underfunding in four of its multiemployer plans would be difficult to replicate for plans in which Kroger is a significant, but not dominant, employer. Special contributions – such as the $650 million contribution Kroger made to the new consolidated plan – would improve the overall funding of the plan but would effectively benefit all contributing employers. However, unless other contributing employers can be persuaded to make special contributions, there is little reason for Kroger to unilaterally fund these plans. To illustrate, if Kroger is an equal participant in a multiemployer plan with

four other employers, 80 cents of every additional dollar Kroger contributes towards the current underfunding would serve to reduce the overall plan liability of other contributing employers, and would actually increase Kroger's share of the plan's remaining unfunded benefits if Kroger were to withdraw.

In the case of the new consolidated plan, Kroger took action only after concluding that because it was already the "last man standing," the advantages of plan consolidation outweighed the cost of the additional contribution dollars. While special withdrawal liability rules and contribution agreements could be fashioned to encourage others contributors to follow Kroger's example, these steps would have to be voluntarily adopted by the plan trustees and cannot completely address all of the impediments to accelerated funding under current law. Unless other contributing employers can be persuaded to make a similar contribution, the current system effectively discourages employers from committing significant dollars to address underfunding in these plans.

V. SUGGESTED CONCEPTS CONGRESS MAY CONSIDER

A. Continue Funding Discipline Inherent in PPA Rules

The Pension Protection Act of 2006 ("PPA") was designed to impose discipline on pension funds and bargaining parties to ensure that the bargaining parties and plan trustees acted responsibly and established reasonable benefit and contribution levels. The PPA also provided needed transparency for multiemployer plans. Prior to PPA, even large employers like Kroger had difficulty securing information about the plans to which they were contributing. Although the PPA included rules requiring funding discipline and additional transparency, it did not change the basic structure of the multiemployer pension plan rules (e.g., withdrawal liability or the "last-man standing" rule).

The PPA rules applicable to multiemployer pension plans are scheduled to sunset at the end of 2014. Congress should act to continue the funding discipline imposed by the PPA by requiring bargaining parties and plan trustees to establish benefits based on available contribution levels, and to eliminate current underfunding over a reasonable period of time. However, the tools currently available to plan trustees, employers and unions wishing to responsibly address plan underfunding issues have proven to be insufficient. The parties will need greater flexibility in order to develop and implement the necessary measures to address the underfunding issue in a mutually satisfactory manner.

B. Greater Flexibility

Multiemployer plans, labor unions and employers are working together to develop policy recommendations that would address the current underfunding of multiemployer plans. Because such a substantial proportion of our workforce relies on these plans to secure their retirement, and because Kroger has had to devote significant resources to fund the benefits of other workers in these plans, Kroger is deeply invested in finding a solution to these challenges. Kroger is committed to being part of the problem-solving process.

What is clear is that multiemployer plans and bargaining parties must be provided with greater flexibility to address the underfunding situation. Given the unique circumstances of each plan, the parties should be afforded as much flexibility as possible. For example, the fortunes of some plans could be improved by encouraging consolidation as a means of promoting greater efficiencies and reducing expenses.

Plan trustees, unions and employers should be encouraged to take responsible steps to place underfunded plans on solid footing. The parties need support and flexibility so they can

determine the best course of action to improve their funding situation. There is no easy solution to this problem, and the way forward is unclear. But solutions exist, and by working together, we can secure the retirement benefits our employees are counting on.

VI. CONCLUSION

Kroger applauds this Subcommittee for its leadership in holding this hearing and beginning the process of addressing the structural problems facing the multiemployer system. We are grateful for the opportunity to tell our story, and we look forward to working with you, the multiemployer plans and labor on a solution that will ensure the continued viability of the multiemployer system.