Regulating Private Pensions: A Brief Summary of ERISA

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Summary

The Employee Retirement Income Security Act of 1974 (ERISA, P.L. 93-406) protects the interests of participants and beneficiaries in private-sector employee benefit plans. It was passed in response to instances in which employers had failed to prudently manage pension funds, had terminated pension plans without sufficient assets to pay the benefits employees had earned, or had created impediments to earning a pension, such as onerous age and service requirements. ERISA covers a number of fringe benefits provided by employers, but most of its provisions deal with pension plans. Pension plans sponsored by the federal, state, and local governments, or by churches generally are exempt from ERISA. (This report will be updated for amendments to ERISA.)

Minimum Standards. ERISA does not require employers to provide pensions, but those that do must meet minimum standards in regard to who can participate, how long a person has to work to be entitled to a pension, and how much funding must be set aside each year by the employer to assure payment of pensions when due. ERISA also created the Pension Benefit Guaranty Corporation (PBGC) to guarantee the payment of pensions in case a financially ailing sponsor terminates a defined benefit pension with insufficient funds to pay promised benefits. (A defined benefit plan is one that promises a future pension based on a formula that typically takes into account length of service and annual earnings.) All firms that sponsor a defined benefit pension must pay insurance premiums to the PBGC. The current premium is $19 per participant per year.

ERISA requires plan sponsors to handle funds prudently and in the best interest of participants and beneficiaries. Plan participants must be informed of their rights and of changes in the plan’s financial status. Plan participants may exercise their rights under the law without harassment or interference, may appeal if they are denied benefits, and may sue in federal court to recover benefits due. ERISA has been amended over the years to provide greater protection to survivors and spouses of pension plan participants, to accelerate sound pension funding, to bolster the financial integrity of the PBGC, to ensure that plan participation is broadly based and does not discriminate in favor of highly compensated individuals or owners, and to shorten the tenure needed for benefit
entitlement (vesting). Defined benefit plans generally may not require more than 5 years of service for pension credits to vest. Employees generally must be fully vested in employer contributions to a defined contribution plan (like a 401(k) plan) in no more than 3 years.

**Internal Revenue Code Provisions.** Congress added minimum standards for pension plans to the Internal Revenue Code at the same time it passed ERISA. To qualify for tax preferences, pension plans must meet not only the standards set by ERISA but additional tax code requirements as well. These tax rules include limits on plan contributions and benefits, special rules for “top heavy” plans that benefit primarily highly compensated individuals and/or business owners, and uniform rules for plan distributions.

**Preemption of State Laws.** ERISA preempts state laws affecting all employee benefit plans. Besides pensions, these other benefits (often called “welfare benefits”) include employer-provided health insurance and life insurance, disability benefits, prepaid legal plans, and apprenticeship and training programs. ERISA preempts state insurance law only for employers that self-insure, which is a common practice among large employers. Health, life, or disability insurance purchased through an insurance company remains subject to state insurance laws. Many small employers purchase health insurance through insurance companies because they are too small to accept the risk of self-insuring.

**Welfare Benefit Plans.** Welfare benefit plans are subject to ERISA’s fiduciary standards if money is set aside to fund those benefits, and they must comply with ERISA’s reporting and disclosure requirements if they cover at least 100 participants. Welfare plans also are subject to claims and enforcement standards. However, there are no minimum participation, vesting, or funding standards, nor are welfare benefits insured by the PBGC.

**Administration.** Responsibility for enforcing ERISA is shared by the Department of Labor and the Internal Revenue Service. Fiduciary standards, and requirements for plan reporting and disclosure are administered through the Department of Labor. Requirements for plan participation, vesting, and funding are enforced by the Internal Revenue Service.

**Additional References**


