STATEMENT

"Retirement Insecurity: 401(k) Crisis at Enron"
Chairman Joe Lieberman

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As prepared for delivery

Welcome to today's hearing of the Senate Governmental Affairs Committee, "Retirement Insecurity: 401(k) Crisis at Enron," our second on the lessons learned from the largest bankruptcy in American history.

Though many of us are still coming to grips with the depth of the damage caused by Enron's collapse, for Enron employees and retirees themselves, the consequences were crystal clear from the day the company crumbled. To put it plainly, they lost their savings. They watched their nest eggs evaporate. They lost trust—in both the personal and fiscal senses of the word—in the system. And millions of other workers around the country who have been following the sad stories of Enron's employees have grown anxious about their own 401(k) accounts and their own retirement security.

Today's hearing will ask exactly what happened to Enron employees' 401(k)s, and what can and should be done to safeguard these investment accounts for the more than 40 million Americans who depend on them for their retirement.

First, let's place the Enron 401(k) story in historical context. Most Americans used to count on traditional defined-benefit pension plans, in addition to their Social Security benefits, to support them in retirement. In those plans, employees' retirement funds are pooled and invested by a professional manager, and a fixed monthly pension is paid out to the employee once he or she retires. The federal government recognized the central role these plans played in the lives of Americans and in 1974 enacted major legislation—called ERISA, the Employee Retirement Income Security Act—to protect pension investments and safeguard them from abuse.

In the early 1980s, private retirement plans underwent a major evolution, as the 401(k) defined contribution plan was developed. For many workers, it was a welcome innovation. The 401(k) offers a number of investment options, including mutual funds and stocks. The money an employee pays into it ultimately becomes theirs to control. Also, it's portable—which is important in our increasingly mobile economy. And perhaps most attractive of all, the 401(k) is an investment that can grow over time. Indeed, in the bull market we experienced for much of the last two decades, it may have seemed to most Americans that any money put into a 401(k) was bound to increase dramatically over the course of a career. Government also encouraged the proliferation of 401(k)s by offering tax deferrals to both employees and employers.

So it's no wonder that today 401(k) plans are very popular—holding 42 million American workers' retirement money, with total assets of almost $2 trillion. An account that was originally intended to be a supplemental source of retirement income has become the very foundation of millions of Americans' retirement plans.

Since the passage of ERISA, retirement security has changed in ways that the law never anticipated. As retirement savings have migrated to 401(k)s, risks have shifted from employer to employee. The Enron debacle reveals how serious those risks can be for typical American workers when mixed with an un-diversified portfolio and corporate deceit and mismanagement. It's time for

the law to catch up with reality and protect our workers' 401(k) retirement plans.

When a 401(k) plan is responsibly managed and its risks and rewards are realistically understood, it is a terrific tool that empowers American workers to build up funds for their future. I would urge all American workers, who have the opportunity, to continue contributing to their 401(k) plans, but I also urge you to make sure you are not investing too much in any one company, including your own.

That said, government must address the real problems that exist with 401(k) plans. In developing a roadmap for reform, our attention is drawn to two issues in particular. First is over-concentration. When shares of Enron were near their highest value just over a year ago, about two-thirds of total 401(k) plan assets were in the company's stock. That's an average—which means that some employees had just about all their nest eggs in the company's basket.

How did that happen? Two big reasons. One, Enron matched employee contributions with substantial amounts of its stock and prohibited employees from shifting that company-contributed stock to a different investment until age 50. Two, the company's culture actively encouraged accumulation of Enron stock. Enron's top management repeatedly promoted its stock through internal publications and communications, even when executives must have known the company was a house of cards. In a meeting on September 26 of last year, then-CEO Ken Lay was still telling his employees that the stock's $27-a-share purchase price was "an incredible bargain." Lay claimed that "[t]he third quarter is looking great," and "[w]e will hit our numbers." Just two weeks later, on October 16, 2001, the company announced it was taking a $1 billion after-tax charge to earnings.

Leaving the question of legality aside for now, it's just plain wrong for executives to enthusiastically recommend their company's stock to workers when they know workers are taking that as encouragement to load up on company stock in their 401(k)s. It's wrong for management to convey in internal communications that the company's stock is on the way up when they have reason to believe otherwise. That's not optimism. It's dangerous deceit.

The problem of 401(k) over-concentration should be particularly troubling to us because it's widespread. Nationwide, employees of companies without stock matching programs have an average of about 20 percent of their 401(k) assets in employer stock. And employees of companies with stock matching programs have an average of about 50 percent of their 401(k) assets in employer stock.

Some people say that if employees are willing to make risky and un-diversified investments in their 401(k) plan, government can't stop them. The creator of the first 401(k) plan, benefits consultant Ted Benna, disagrees. He says, "We require auto passengers to wear seatbelts because many won't wear them voluntarily. We should also protect employees from financial disaster by prohibiting them from investing all their retirement savings in a single stock."

The second major issue we're going to focus on is what's known as the "lock-down" period. In late October and early November of last year, because Enron was changing the outside administrator of its 401(k) plan, employees were locked into their 401(k) accounts for at least two weeks during a volatile period in the company's stock price, making them powerless to sell their Enron stock as it was dropping. That left many of them feeling like their hands were tied to the deck of a sinking ship, and they were.

The thought of employees sustaining huge losses while executives were able to

sell stock for millions is infuriating—and especially infuriating because it was preventable. The risk of a catastrophic loss in the value of a 401(k) account occurring during a lock-down increases exponentially when employees have most of their assets invested in a single stock. And when that stock is in the employer itself—as it was in Enron's case—the risk of such a loss occurring, and the risk of other conflicts of interest arising, is even more problematic.

In other words, the danger of a lock-down is multiplied many times over when employees' investments are not diversified.

In Enron's case, management knew full well that their employees' 401(k)s were overloaded with shares of Enron. Shouldn't that have prompted them to postpone the lock-down when the company was reeling?

Recently, legislative proposals have been made which address these problems of over-concentration and lock-downs.

Last week, President Bush put forward a proposal under which employees investing in 401(k) plans would get access to professional investment advice; receive quarterly notices of their pension accounts; be allowed to sell company stock received through a matching program after three years; and receive notification at least 30 days before a lock-down period. His plan would also force senior executives to hold onto their stock during an employee lock-down and allow employers to be held responsible for failing to act in the best interest of their workers during a lock-down.

While I welcome the President's plan as a step forward, I believe it falls far short of what American workers deserve. By focusing so much on the lock-down and ignoring the core problem of over-concentration, the President has over-concentrated on the straw that may have broken the camel's back—not on the bales of hay that were weighing it down in the first place.

Remember, Enron stock had plunged by up to $75 per share from its high before the lock-down even began. The 401(k) plans of Enron employees were vulnerable before, during, and after the lockdown because they were over-invested in a single stock. The President's plan touches on over-concentration, but only by allowing workers to diversify the stock they have received through employer matches. That's a very small piece of the overall problem, so I hope we can work together to develop a more effective proposal to protect the retirement security of America's workers.

Shortly, I will introduce my own plan to safeguard employee retirement plans. I hope that it will make a constructive contribution to our bipartisan efforts to offer employees the protection they deserve.

Improving the security of 401(k)s couldn't be a more pressing priority. To many Americans, the "three-legged stool" of retirement security—made up of Social Security, private pensions, and personal savings—is starting to look wobbly. With the stability of Social Security in long-term jeopardy because of the growing federal deficits and personal savings rates at just 1.1 percent, we need to get 401(k) reform right.

We have a great group of witnesses today who can help us do that. I look forward to hearing from our panels—, from those who experienced Enron's demise first-hand; from the Enron managers and others who helped run the 401(k) plan; and from the policy experts who will suggest ways to protect other American workers from a similar disaster.

Thank you. Senator Collins?

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