Senate Republicans Release Proposal for Multiemployer Pension Reform

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On November 20, Republican Senators Charles Grassley and Lamar Alexander – chairmen of the committees with jurisdiction over pensions – jointly released the *Multiemployer Pension Recapitalization and Reformation Plan* (the "Proposal"), which is a far-ranging proposal for amending the rules governing multiemployer pension plans. The Proposal consists of two documents. The first is a White Paper that discusses the current environment, the rationales behind the Proposal, and the key provisions. The second document is the Technical Explanation, which provides a detailed discussion of current law and the modifications that the Proposal would make. Thus far, no legislative language implementing the Proposal has been released.

The primary impetus for the Proposal is the impending insolvency of over 100 multiemployer pension plans covering more than a million participants and the projected insolvency of the multiemployer insurance program administered by the Pension Benefit Guaranty Corporation ("PBGC"). In addition to addressing failing plans, the Proposal contains a series of measures that are intended to ensure that additional crises do not occur in the future. The scope of these measures is extremely broad, and they would affect nearly all aspects of multiemployer plan funding, administration, and governance.

Background

There are currently roughly 130 multiemployer pension plans that are projected to fully exhaust their assets within the coming 20 years. These plans represent over 10% of the entire multiemployer system, and they cover more than a million active, inactive, and retired workers.

When a multiemployer plan becomes insolvent, PBGC provides the plan with financial assistance to allow it to continue to pay benefits up to the statutory guarantee level. This guarantee level is relatively low, covering at most roughly $1,100 per month for a full-career employee with 30 years of service. Plans pay an annual premium to PBGC ($29 in 2019) per participant to support this guarantee.

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The PBGC multiemployer insurance program itself is seriously underfunded, and is projected to exhaust its resources in approximately 6 years.[1]

Employers contribute to multiemployer plans based on rates set by collective bargaining, which often require a specified amount to be paid into the plan per hour (or other unit of employment) of covered work. Federal law generally requires that the bargaining parties negotiate contribution rates that will be sufficient to fully fund plans over a period of 15 years, though there are exceptions for plans that cannot reasonably meet this standard. The actuarial assumptions used to measure the plan liabilities for minimum funding purposes are based on the actuary's best estimate of future experience. The actuarial assumptions include an expected rate of future investment return. There is a significant amount of variation on a plan-by-plan basis in the expected rate of future investment return, but many plans assume approximately 7.5% per year.

When an employer ceases contributing to a plan that is less than fully funded, it is generally assessed withdrawal liability, which is a proportional share of the plan's underfunding. The employer generally is not obligated to pay the withdrawal liability assessment as a single sum; rather, it has the option of making payments under a statutory payment schedule. The amount of the annual withdrawal liability payment depends on the employer's contribution history and is independent of the amount of liability allocated. Withdrawal liability payments continue until the earlier of (a) when the assessment is fully paid off, or (b) 20 years. In the event substantially all employers withdraw from a plan, the 20-year cap may be lifted.

Key Provisions of the Proposal

The Proposal would make extensive changes to the rules governing multiemployer pension plans. The following summary is based on the Technical Explanation of the Proposal. There are some areas of the Proposal that are not fully clear based on the information available in the Technical Explanation and White Paper, and due to the lack of legislative language.

Partition of Insolvent Multiemployer Pension Plans

The Proposal would address failing multiemployer plans by allowing them to transfer a portion of their liabilities to a new plan that would be supported by PBGC in a process known as a partition. The goal is to reduce the liabilities of the original plan such that it is financially viable. Partitions exist under current law, but the circumstances in which they can occur are narrow, and they have not been used extensively because of PBGC's financial condition. The special partition provisions in the Proposal would be temporary, with a 12-month window following enactment in which eligible plans could apply under the new rules.

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[1] Under current law, PBGC does not receive any funding from the U.S. Treasury. If its multiemployer program exhausts its assets, the guaranteed benefits likely would decrease to a level the agency could afford on a pay-as-you-go basis from premium receipts, which would be a small fraction of the current guarantee level.

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In order to be eligible for a special partition, a plan would need to (a) be in critical and declining status as of the date the Proposal was released (*i.e.*, November 20, 2019), (b) have implemented a suspension of benefits under the Multiemployer Pension Reform Act of 2014 ("MPRA"), or (c) be in critical status with a funded ratio below 40% on a current liability basis and a ratio of active participants to inactive participants of 40% or lower.[2] Additionally, a small number of plans would be automatically eligible and special rules would apply to those plans.

In order to receive a special partition, plans must have taken all reasonable measures to avoid insolvency, including reducing the rate of monthly benefit accrual to be no more than 1% of annual contributions as of the first day of the first plan year after enactment. The Proposal also appears to require that partitioned plans implement MPRA benefit suspensions equal to 10% of the current benefit levels, subject to certain protections for older and disabled participants.

A special partition would transfer the amount of liability that is necessary for the original plan to remain solvent indefinitely. If a partition of 100% of the benefits up to the PBGC guarantee level is insufficient to allow a plan to remain solvent, then the plan would not be eligible for a special partition under the Proposal. The Proposal calls for such a plan to engage in restructuring discussions with PBGC, but the extent of PBGC's authority in this situation is unclear.

The new plan created by the partition would receive funding from PBGC in an amount necessary to support benefits up to the PBGC guarantee (which would be increased above current levels under another provision in the Proposal). Any benefits owed to participants in the newly created plan that are above the PBGC guarantee would be paid by the original plan. In the event an employer withdraws from a plan within 15 years of a special partition, the withdrawal liability calculation would disregard the impact of the partition, and a 25% surcharge would apply to the annual withdrawal liability payment amount.

PBGC Guarantee Level

Currently the PBGC guarantee covers 100% of the first $11 of a participant's monthly benefit accrual rate, plus 75% of the next $33 dollars of the accrual rate. For a participant with 30 years of service, this formula results in a maximum guaranteed benefit of $1,072.50 per month, or $12,870 per year.

The Proposal would increase the PBGC guarantee formula to 100% of the first $56 of monthly benefit accrual, with no guarantee for benefit accruals above this rate. A participant with 30 years of service would have a maximum guaranteed benefit of $1,680 per month, or $20,160 per year. In no event would the guarantee be less than $250 per month. As under current law, benefit increases that are in effect for less than 5 years would not be guaranteed by PBGC.

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[2] Current liability is a measurement of a plan's liabilities using a discount rate that is based on 30-year Treasury securities and is currently below 3%.

PBGC Insurable Event

Under current law, PBGC generally only provides financial assistance to multiemployer plans after they fully exhaust their assets. Benefits are reduced to the PBGC guarantee level at that time. Insolvent plans are not explicitly required to freeze benefit accruals, meaning it may be possible for participants to continue to accrue benefits at the PBGC guarantee level after PBGC begins to pay financial assistance.

Under the Proposal, once a plan is projected to be insolvent within five years, it is required to freeze all benefit accruals and reduce participant benefits to the PBGC guarantee level. These provisions would apply to plans that do not receive partitions under the terms of the Proposal. The Proposal would also provide that plans from which all employers have withdrawn, or that have been amended to freeze all benefit accruals, must reduce benefits immediately to the PBGC guarantee level unless they are fully funded.

PBGC Premiums

Plans currently pay annual premiums to PBGC equal to $29 per participant, including active, inactive, and retired participants. This amount is indexed to inflation, and is scheduled to increase to $30 in 2020. The Proposal would increase this amount to $80 per participant. Additionally, the Proposal would implement a new premium on both the employers that contribute to the plan and on the unions that represent the covered employees. These new premiums are both equal to $2.50 per month (*i.e.*, $30 per year), per active employee covered by the plan.

The Proposal would introduce a new variable rate premium that would be paid by multiemployer plans. This premium would be equal to 1% of the unfunded liability of the plan, measured on a current liability basis. Current liability is determined based on the yields on 30-year U.S. Treasury bonds, and is typically a much higher liability measurement than is used for other purposes. The per-participant variable rate premium would be capped so that it cannot exceed the lesser of the average benefit amount payable from the plan, or $250 per plan participant.

The Proposal would also introduce a new premium that would be paid from amounts withheld from retiree benefit payments. The amount withheld and paid to PBGC as a premium would depend on the financial condition of the plan. The largest premiums would be withheld from the benefits of retirees in plans that have been partitioned, where a 10% premium would apply. Retirees in plans in declining status and frozen plans would be subject to 7% premiums, retirees in critical status plans would be subject to 5% premiums, and retirees in endangered plans would be subject to 3% premiums. Plans not in any of these conditions would not be required to withhold any amounts from retiree benefit payments.

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Valuation of Pension Liabilities for Minimum Funding Purposes

For purposes of determining minimum funding requirement, federal law currently requires that plan actuaries measure multiemployer pension liabilities using a discount rate that represents their best estimates of anticipated returns on plan assets. The most commonly chosen assumption for this purpose is 7.5% per year, and more than 90% of plans have an assumption that is greater than 6%.

Under the Proposal, the discount rate used for minimum funding purposes would be the lesser of the actuary's best estimate or a statutory cap. The cap would be equal to the lesser of (a) the 24-month average of the 3rd segment rate used for single-employer plan minimum funding purposes, plus 200 basis points, or (b) 6.00%.

As of November of 2019, the 3rd segment rate is 4.33%, and with 200 basis points added the rate is 6.33%. Thus, in the current economic environment, the maximum discount rate for determining multiemployer plan funding requirements would be 6% (*i.e.*, the lesser of 6.33% and 6.00%). Since a large majority of plan actuaries currently assume higher rates of return, the Proposal would cause most plans to use a lower discount rate, which in turn would raise the measured liabilities.

The discount rate cap would be phased in over 5 years, though the exact mechanism of the phase-in is not clear. Additionally, the increase in liabilities that is attributable to the new discount rate rules would be amortized over 30 years.

As a result of the lower discount rates, most plans would report lower funding levels than they do under current law. The impacts of this change would include higher minimum funding requirements, plans being in a less favorable zone status, and larger contribution increases or benefit cuts needed to emerge from a zone status. It is likely that there would also be an increase in the number of plans concluding that they have exhausted all reasonable measures and are unable to emerge from critical status.

Zone Status Definitions

Federal law currently classifies multiemployer plans as either being in critical status or endangered status, with a default category of plans that do not meet the criteria for either critical or endangered status. In general, a critical status plan is one that has either failed to satisfy the minimum funding requirements, or is projected to do so within 4 years. An endangered status plan is one that either has a funded ratio below 80%, or is projected to fail to satisfy the minimum funding requirements within 6 years. A critical status plan that is projected to fully exhaust its assets within 20 years is further classified as a critical and declining status plan.

The Proposal would revise the zone status framework to include the following statuses:

- *Unrestricted Status* – Funded ratio projected 15 years into the future is at least 115%, or current liability funded percentage is at least 80% for the current plan year (also shown as 70% in a chart in the Proposal)

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- *Stable Status* – Plan does not meet the requirements for any other zone status
- *Endangered Status* – Funded ratio is below 80%, or plan is projected to fail to satisfy the minimum funding requirements in 9 years
- *Critical Status* – Funded ratio is below 65%, or plan is projected to fail to satisfy the minimum funding requirements in 6 years, or the funded ratio projected 15 years into the future is less than 80% (note that a chart in the Proposal omits the third of these criteria)
- *Declining Status* – Plan is projected to fully exhaust its assets within the coming 29 years, or is (a) not projected to ever emerge from critical status and (b) has a funded ratio projected 15 years into the future that is lower than the current funded ratio.

Zone Status Rules

Other than continuing to comply with the minimum funding rules, plans that are in either unrestricted or stable status would not be required to take any additional steps to improve their funding levels. These plans would be permitted to improve benefits, subject to some restrictions regarding the impact that the improvement would have on the zone status.

Endangered status plans would be required to develop and implement a funding improvement plan that is designed to enable the plan to emerge from endangered status over a 10-year timeframe. This is a departure from current law, where funding improvement plans must be designed to achieve specified funding benchmarks, but do not need to target emergence from endangered status. These plans would be permitted to adopt benefit improvements, provided the improvement is funded by additional contributions that are not contemplated by the funding improvement plan.

As under current law, critical status plans would be required to adopt a rehabilitation plan that is designed to allow the plan to emerge from critical status over a 10-year period. If the plan is not projected to meet this standard after exhausting all reasonable measures, then it must adopt reasonable measures to emerge from critical status at a later date or to forestall insolvency. A plan that is not projected to emerge from critical status by the end of the 10-year period would not be able to have a monthly accrual rate that exceeds 1% of annual contributions based on the current contribution rate. Critical status plans would not be permitted to adopt benefit improvements unless the impact of the improvement is *de minimis*, or if it is required by law.

Under the Proposal, declining plans would be subject to the same benefit improvement restrictions as critical plans. These plans must adopt a solvency plan, which is similar to a rehabilitation plan that avoids or forestalls insolvency under current law. Declining plans would not be able to have a monthly accrual rate in excess of 1% of annual contributions based on the current contribution rate, and any contribution rate or compensation increases must be excluded from benefit formulas that are based on contributions or compensation. Similar to current law, declining plans would be able to apply for benefit suspensions, as provided under MPRA.

Plans in unrestricted or stable status would be permitted to accept collective bargaining agreements that provide for decreases in contribution rates, provided the decreased rates do not put the plan into a

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status below stable. Other plans would only be permitted to accept reduced contribution rates if they are accompanied by a comparable reduction in benefit accruals, or if the trustees determine that accepting the lower rates serves the best interests of plan participants.

The Proposal would largely maintain the current rules regarding adjustable benefits, with two significant changes. First, plans in endangered status would be permitted to reduce adjustable benefits, instead of only critical status plan as under current law. Second, benefit improvements that have been in effect for less than 10 years would be considered to be adjustable benefits, as opposed to 5 years under current law.

Withdrawal Liability

Under the Proposal, the annual amount that a withdrawn employer would be obligated to pay to a plan is the product of (a) the highest level of employment (most often measured in hours of work) the employer has had in the plan over the past 20 years, and (b) the highest contribution rate under which the employer has contributed over the past 10 years. This calculation would be subject to a floor that is equal to the highest dollar amount of contributions over the prior 20 years.

The withdrawal liability payment amount formula is similar to current law, except that under current law the look-back period for the highest level of employment is 10 years instead of 20 years. Additionally, under current law a 3-year average of the employment level is used for this purpose; it is not clear if the Proposal would maintain this average or move to a single highest year approach.

The duration of the withdrawal liability payment schedule would be based on a formula that depends on the funded ratio as determined using the same interest rate assumption used under the minimum funding rules. If the funded ratio equals or exceeds 140%, then no withdrawal liability payments are due. If the funded ratio is 90% or better, but less than 140%, then 5 years of withdrawal liability payments are due. For every 2 percentage points below 90% funded, a withdrawing employer owes one additional year of withdrawal liability payments. For example, an employer that withdraws from a plan that is 70% funded would owe 15 years of withdrawal liability payments. The maximum payment schedule duration would be 20 years, unless the plan is in declining status or is terminated, in which case the maximum duration would be 25 years.

In contrast with current law, no special provisions would apply when all or substantially all employers withdraw (*i.e.*, a mass withdrawal). In the event the funded ratio is at least 100% but less than 140%, no withdrawal liability would be due if the plan has a policy of immunizing or annuitizing the employer's share of the liabilities. The building and construction industry exemption would continue to apply, provided the plan amortizes unfunded liabilities that arise after enactment over a period of 10 years. Plans would not be permitted to settle withdrawal liability assessments for less than the present value of the withdrawal liability payment schedule measured at the minimum funding discount rate, unless the trustees determine that it is appropriate solely based on the financial health of the withdrawn employer.

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Governance

The Proposal would make several changes relating to the governance of multiemployer plans. Any plan that receives relief from the special partition program would have an independent trustee appointed by PBGC. This trustee would have monitoring duties and some ability to override board decisions, though the scope of this ability is not clear. PBGC could add an independent trustee to the existing board, or seek a court order to replace the existing board with an independent trustee if it believes the board has mismanaged the plan.

Trustees of plans that receive special partitions would be subject to 10-year term limits, and the executive directors of these plans would be subject to 12-year term limits. There would also be an excise tax on compensation above $500,000 for the top-paid 5 employees of partitioned plans.

Under the Proposal, PBGC would be able to petition a court to terminate a critical or declining status plan, if it concludes this step is necessary to protect participants or PBGC. PBGC would also have the ability to investigate troubled plans, and to initiate mergers of small terminated or insolvent plans. The proposal would also direct PBGC to establish a reportable event framework for multiemployer plans, and would revise the rules regarding annual funding notices and zone status notices.

MPRA Benefit Suspensions

Under MPRA, benefit suspensions are generally only implemented after they are ratified in a participant vote. Specifically, current law provides that benefit suspensions that have been adopted by the trustees and approved by the Treasury Department will go into effect unless a majority of all participants vote against the suspensions. In this framework, a participant who does not vote is effectively identical to a participant who votes in favor of the suspensions, since all that matters is the absolute number of votes against the suspensions. In addition, under current law the Treasury Department may override a participant vote rejecting a suspension for certain systemically important plans. The Proposal would change the voting procedures such that a majority of the votes received must be in favor of the suspensions in order for them to go into effect.

Current law requires that benefit suspensions be projected to allow a plan to remain solvent indefinitely. The Proposal would change the solvency requirement to a 65% chance that the plan will remain solvent for 20 years. It would also make it clear that once the Treasury Department provides notice and a comment period through the Federal Register, it would not be necessary to repeat this process for *de minimis* changes to a suspension application. Lastly, the Proposal would establish a flat, across the board reduction percentage as a safe harbor for equitable distribution purposes, and would extend the existing protections for participants receiving disability benefits under a plan to all participants who have qualified for Social Security disability benefits.

Composite Plans

The Proposal would authorize a new type of retirement plan that is commonly referred to as a composite plan. A composite plan would operate much like a current defined benefit plan, except that

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employers' financial obligation to the plan would be limited to the bargained contributions. To the extent that underfunding develops that cannot be addressed through increased contributions or reductions in future benefit accruals, participants' accrued benefits would ultimately be adjusted in order to balance the obligations with the available resources. Composite plans would have no withdrawal liability or PBGC guarantees.

The funding standards for composite plans would be based on a projection of the assets and liabilities, and plans would be required to maintain a projected funded ratio of at least 120%. A composite plan could be a component of an existing defined benefit plan, but separate asset pools would be strictly maintained. A current defined benefit plan would not be permitted to implement a composite plan if it is in critical or declining status.

If a composite plan fails to satisfy the 120% projected funded ratio standard, it would be required to develop and implement a realignment program to address the failure. A realignment program must first attempt to improve funding levels through increases in the contribution rates that are negotiated by the bargaining parties, reductions to future benefit accruals, and modifications to ancillary benefits. If these measures are insufficient, then the plan would be allowed to reduce accrued benefits to non-retired participants and ancillary benefits to retired participants. If these measures are also insufficient, then the plan would be able to reduce core benefits to retired participants.

If a legacy defined benefit plan implements a composite plan, it would be required to calculate a transition contribution rate that is expected to fully fund the liabilities over 25 years. Any subsequent adverse experience would be amortized over 15 years and added to the transition contribution rate. Employers would be required to contribute at least the transition contribution rate to the legacy plan, and could only claim that all reasonable measures to improve funding have been taken if 75% or more of the total contributions between the legacy and composite plans are going to the legacy plan.

Next Steps

Senate Republicans have devoted an enormous amount of time into developing the Proposal, and there is every indication that they expect to use it as the basis for negotiations with Senate and House Democrats. It is likely that both Democrats and various stakeholders in multiemployer plans will object to some provisions of the Proposal, and it remains to be seen whether compromises can be reached and over what timeframe. Earlier this year, the House passed the *Rehabilitation for Multiemployer Pensions Act of 2019* (H.R. 397) with some Republican support (29 votes). The Proposal has essentially no overlap with the House-passed legislation.

At this point, it is difficult to predict whether Congress will act, but the Proposal is likely to have a significant influence on the process going forward. Multiemployer plans, and the employers and unions that participate in them, should consider performing analyses of the effects the Proposal would have on funding requirements, benefit levels, and plan governance. This analysis will help ensure that all parties are prepared for the changes that might occur and, perhaps more importantly, will put

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stakeholders in a position to provide valuable feedback to policymakers as they work to finalize a reform package.

Some specific questions that plans might want to consider analyzing are as follows:

- Would the plan be eligible for a special partition, and if so, how much liability is likely to be partitioned?
- What would the new premium structure mean for plans, employers, and participants?
- How would the change to minimum funding discount rates affect the plan's funded ratio and contribution requirements?
- What zone status would the plan fall into?
- How would withdrawal liability assessments be affected?
- Would transitioning to a composite plan meet the needs of employers and employees more effectively than the current plan?