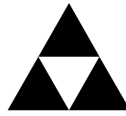


AMERICAN ACADEMY *of* ACTUARIES

March 4, 2004

David Thompson
Labor Counsel
Senate Committee on Health,
Education, Labor and Pensions
SH-608
Washington, DC 20510

Portia Wu
Labor Counsel
Senate Committee on Health,
Education, Labor and Pensions
SH-639
Washington, DC 20510

Re: HR 3108 – Multiemployer provision

Dear Mr. Thompson and Ms. Wu,

On behalf of the American Academy of Actuaries'[1] Pension Practice Council, I appreciate the opportunity to submit the following comments, prepared by the council's Multiemployer Plans Task Force, on the multiemployer provisions of HR 3108, as passed in amended form by the Senate in January.

Relief of this nature is critical for many multiemployer plan sponsors. It would allow trustees additional time to resolve the continued financial strain these plans are experiencing through a combination of contribution increases (in conjunction with one or more collective bargaining cycles) and benefit level adjustments. The current crisis was brought about by recent economic experience following restrictive tax regulations that prevented the development of strong funding margins in the 90s. The additional relief under the Senate version of the legislation will provide needed time for the bargaining parties to restore the balance between benefits and financial resources. Without relief, some pension plans' current minimum funding requirements would result in significantly more drastic benefit cuts and/or contribution increases in the near future and may make employers who are meeting their obligation under existing contracts subject to excise taxes.

The task force's review and technical analysis of Section 5 "Amortization Hiatus for Net Experience Losses in Multiemployer Plans" identified certain potential concerns with the relief structure. References below are to newly created sub-paragraph F under the Internal Revenue Code (IRC) section 412(b)(7).

1. The identification of the specific losses eligible for relief is inserted as clause (i), but the applicable losses eligible for deferral are not clear. The wording "a net experience loss *for any plan year* beginning after June

[1] The American Academy of Actuaries is the public policy organization for actuaries of all specialties within the United States. In addition to setting qualification standards and standards of actuarial practice, a major purpose of the Academy is to act as the public information organization for the profession. The Academy is nonpartisan and assists the public policy process through the presentation of clear actuarial analysis. The Academy regularly prepares testimony for Congress, provides information to federal and state elected officials, regulators and congressional staff, comments on proposed federal and state regulations and legislation, and works closely with state officials on issues related to insurance. The Academy also develops and upholds actuarial standards of conduct, qualifications and practice, and the Code of Professional Conduct for all actuaries practicing in the United States.

30, 2002 and before July 1, 2006" should be clarified. The applicability of the relief concerns actuaries responsible for certification of the minimum funding standards. Does it refer to the loss that was incurred in the indicated year (and first recognized in the following year's actuarial valuation)? Is it the loss first recognized in the actuarial valuation in that year? Or is it the remaining portion of any and potentially all experience losses from prior years that are still being charged to the funding standard account in the relevant year?

In order for the relief provision to be applied timely, work properly, and be simple to administer, the task force suggests that the second interpretation should be codified. The italicized phrase above should be replaced by "…*first recognized in the funding standard account in a plan year*…." This interpretation would also allow plans to elect to use this relief provision for virtually all Form 5500 filings with a due date (with extension) that has not yet passed. Based on limited modeling done by members of the task force, the effect of this interpretation on the funding standard account is expected to be modest, though possibly crucial to preservation of a credit balance until the end of the current collective bargaining agreement for plans most in need of relief.

2. During a hiatus in which amortization payments are deferred, interest using the actuary's best-estimate funding rate would normally be expected to accrue in the funding standard account. But the legislation provides that interest is instead charged to a reconciliation account under clause (v) until amortization begins. It is important to clarify whether — and how — this accumulated interest amount is charged to the funding standard account at the end of the hiatus period. Simply leaving the accumulated amount in the reconciliation account means that the interest cost of the deferred experience loss is never incorporated into the minimum funding requirements. Some multiemployer plan actuaries are concerned with this aspect and feel there should be a provision for this interest charge to be brought back into the funding requirement at some point in time, while others are not concerned about this form of "permanent" relief.

   The relief is expected to be useful, especially in the initial few years, for the most troubled plans needing additional time to solve their funding problems, whether or not the accumulated three years of interest is incorporated after the hiatus. At the end of a three-year hiatus, recognition of the interest accruing on the deferred loss can be accomplished by adding the reconciliation account to the original amount of deferred experience loss. The result of including interest at the valuation rate could be either a larger annual amortization payment (about 25 percent larger) or a longer period of amortization with the same initial payment amount (roughly 8 years longer), rather than leaving the amount in the reconciliation account. Either approach would be reasonable. As currently drafted, only the former applies, but use of the latter would help preserve far more of the near-term benefits of the intended relief, while maintaining actuarial funding principles.

   While suspension of interest is quite unusual in the operation of the funding standard account, current relief mechanisms in IRC 412(d) and (e) (with respect to waivers and amortization extensions available from IRS) mandate use of a short-term interest rate for amortization, as well as deferral purposes. That alternative short-term interest rate might be used for accumulating interest in the funding standard account during the hiatus outlined by this legislation. This legislation provides a readily accessible method of funding relief, versus the existing relief measures that entail long applications and often protracted regulatory reviews.

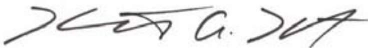
3. Constraints apply to a plan's ability to adopt amendments that increase benefits during the hiatus. As specified in clause (ii)(I), the prohibition can be overcome by a projection that the funded current liability percentage (under 412(l)(8), including the effect of the amendment) as of the end of the plan year is at least 75 percent. We suggest the Enrolled Actuary be made responsible for this projection, to be certified within the Form 5500 / Schedule B filing for the year of adoption.

We also suggest that the second option provided under (ii)(II) for overcoming the benefit improvement restraint (an actuarial certification that the incremental annual contribution income, presumably from higher rates first effective during or after the same year as the benefit increase is adopted, covers the sum of the increase to normal cost plus 3 to 6 year amortization of the increase to the accrued actuarial liability, in the first full plan year) be certified by the Enrolled Actuary within the Form 5500/ Schedule B filing for the year of adoption.

4. Finally, we suggest that plans electing to use the relief be allowed to discontinue that relief, by reverting to the current funding standard. A reasonable method of accomplishing that would be to require the plan to charge the entire balance in the reconciliation account to the funding standard account in the year the relief is discontinued, and commence immediate amortization of any deferred experience loss currently in the hiatus. Another consequence might be to shorten the outstanding amortization period for deferred losses, ending at the same point as the original 15-year period without relief. This might be a more practical alternative to the disqualification sanction in subsection (b)(2) of the relief measure.

The Academy's Pension Practice Council and Multiemployer Plans Task Force appreciate the opportunity to comment on this legislation and look forward to being of further assistance to you and others concerned with public policy measures affecting multiemployer pension plan financing. If you would like to discuss these comments, please feel free to contact me (202-331-2528; ken.kent@mercer.com) or Heather Jerbi, the Academy's pension policy analyst (202-785-7869; Jerbi@actuary.org).

Sincerely,



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