Introduction
On behalf of the Pension Practice Council of the American Academy of Actuaries, I appreciate the opportunity to provide the following responses for the record to questions provided to us pursuant to the United States House Committee on Education and Labor, Subcommittee on Health, Employment Labor, and Pensions hearing, “The Cost of Inaction: Why Congress Must Address the Multiemployer Pension Crisis,” on March 7, 2019. It was evident to me that all the witnesses believe that the cost of inaction is significant.

Thank you again for the opportunity to provide input to the subcommittee. The Pension Practice Council of the American Academy of Actuaries looks forward to continuing to provide objective and unbiased actuarial analysis to Members of Congress and their staffs as they work to address these difficult challenges.

Sincerely,
Josh Shapiro, MAAA, FSA, EA
Vice President, Pensions
American Academy of Actuaries

Questions submitted on March 20, 2019:

Question #1

Have the changes to single employer plan funding rules, including the use of market rates to discount liabilities, under the Pension Protection Act of 2006 resulted in greater retirement security for participants of single employer plans?

The use of market rates to measure the liabilities of single-employer defined benefit pension plans has contributed to the fact that funding levels in these plans are higher than in multiemployer plans, enhancing the security of single-employer pension benefits. However, those same funding rules have made traditional pension plans more expensive and created volatility in the contribution requirements. Pension Benefit Guaranty Corporation (PBGC) premiums for single-employer plans have also increased dramatically under a series of legislative...
changes. These factors may have contributed to a trend away from employer sponsorship of these plans. This trend has continued even though the market discount rate requirements of the Pension Protection Act (based on high-grade corporate bond yields) have not been fully implemented, as various rounds of legislative interest rate “stabilization” efforts, as well as other relief provisions, have been in effect since 2010.

As a result of the trend away from traditional single-employer defined benefit plans, many of these plans are either closed to new entrants, are frozen (meaning that employees are not earning any new benefits), or have been terminated. 401(k) and similar benefit programs, which have become increasingly prevalent in recent years, routinely expose employees to the possibility of accumulating insufficient assets for a secure retirement. Retirees from these plans—who may be ill-equipped to manage their assets effectively in retirement—are at risk of fully exhausting their assets and being left in poverty.

Market-related discount rates have increased the security of single-employer pension plans relative to multiemployer plans. However, any examination of this issue needs to consider the effects on continued plan sponsorship, which could potentially offset the retirement income security improvements attributable to market-related discount rates.

**Question #2**

**How do multiemployer actuaries set the discount rate for multiemployer plan liabilities for funding purposes?**

a. What goes into that determination?

b. Does that approach comply with actuarial standards of practice in the US?

For minimum funding purposes, the Employee Retirement Income Security Act (ERISA) §304(c) requires the use of “reasonable actuarial assumptions that take into account the experience of the plan and reasonable expectations and offer the actuary’s best estimate of anticipated experience under the plan.” The actuary’s best estimate of anticipated investment return experience is generally based on the plan’s asset allocation (reflecting the plan sponsor’s risk preferences) and the current capital market outlook for each asset class provided by either the plan’s actuary or its investment advisor, taking into account volatility and correlations among the asset classes—as well as historical performance over extended periods.

The Actuarial Standards Board (ASB) promulgates actuarial standards of practice (ASOPs) for use by actuaries when rendering actuarial services in the United States. ASOP No. 27 is the standard used when selecting economic assumptions, including the discount rate, for various measurement purposes. ASOP No. 27 states that the actuary should consider the purpose of the measurement when selecting a discount rate, and consistent with the statutory requirements, the standard specifically lists contribution budgeting as an instance where the rate of anticipated investment return may be an appropriate discount rate. Accordingly, for funding purposes, in our experience multiemployer plan actuaries generally use expected long-term rates of investment earnings to discount liabilities, which they believe complies with the applicable standard of practice.
Question #3

Dr. Naughton indicated that multiemployer plans have not collected “actuarially sound” contributions from contributing employers.

a. What does that mean?
b. Is the system itself sound?
c. What should Congress consider to improve the viability of the system?

There is no universally accepted definition of the phrase “actuarial soundness.” In fact ASOP No. 1 states:

“The phrase ‘actuarial soundness’ has different meanings in different contexts and might be dictated or imposed by an outside entity. In rendering actuarial services, if the actuary identifies the process or result as ‘actuarially sound,’ the actuary should define the meaning of “actuarially sound” in that context.”

The multiemployer pension system covers more than 10 million participants nationwide. Although the majority of these participants are in plans that do not currently face funding distress, roughly 1.3 million participants are in plans that are projected to exhaust their assets in the coming 20 years.

Many stakeholders have traditionally viewed these benefits as being promises not subject to a meaningful risk of reduction. These benefits have been perceived to be more secure than they actually are, since in fact more than 10 percent of participants are in plans that will be unable to pay all the benefits participants have earned. As Congress works to resolve this disconnect, it is important to understand the relationship that exists between benefit security and benefit adequacy. Any measure that makes benefits more secure will tend to make them smaller. As with all financial systems, it is necessary to balance predictability against the potential for gains.

There are multiple approaches that Congress might consider to better align the actual and perceived security of multiemployer pension benefits. For example, benefit security could be strengthened by implementing stricter funding and withdrawal liability rules, or by requiring that investment gains be retained as a cushion against future losses (rather than being used to fund benefit increases). Alternatively, improved mechanisms for adjusting benefits incrementally as necessary could prevent catastrophic reductions, while enhanced participant disclosures would help raise awareness of the risks. In weighing these alternatives, Congress should consider the need for balance between improving benefit security and ensuring that employers and employees are willing and able to sustain retirement plans that provide lifetime income.