

THE MULTIEMPLOYER PENSION CRISIS

Session 3: Strengthening the System for the Future



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Introductions



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About the Academy

- The American Academy of Actuaries is a 19,500-member professional association whose mission is to serve the public and the U.S. actuarial profession. For more than 50 years, the Academy has assisted public policymakers on all levels by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.



Today's Presenters

- **Linda Stone, MAAA, FSA (moderator)**
Senior Pension Fellow
- **Christian Benjaminson, MAAA, FCA, FSA, EA**
Vice Chairperson, Multiemployer Pension Plans Committee
- **Jason Russell, MAAA, FSA, EA**
Chairperson, Multiemployer Pension Plans Committee
- **Josh Shapiro, MAAA, FCA, FSA, EA**
Vice President, Pension



A Three-Part Series

- **Session 1: Background and Current State**
Monday, July 15, 2019 | Noon to 1 p.m.
2261 Rayburn House Office Building
- **Session 2: Possible Approaches for Addressing Failing Plans**
Monday, July 22, 2019 | Noon to 1 p.m.
G11 Dirksen Senate Office Building
- **Session 3: Strengthening the System for the Future**
Friday, August 2, 2019 | Noon to 1 p.m.
485 Russell Senate Office Building

Today's
Session



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Agenda

- Background
- Plan Governance
- Funding Rules
- Benefit Design
- Withdrawal Liability
- Role of PBGC



Background

For more background information, please refer to materials from Session 1.

https://www.actuary.org/sites/default/files/2019-07/MEP_Hill_Briefing_Session1.pdf



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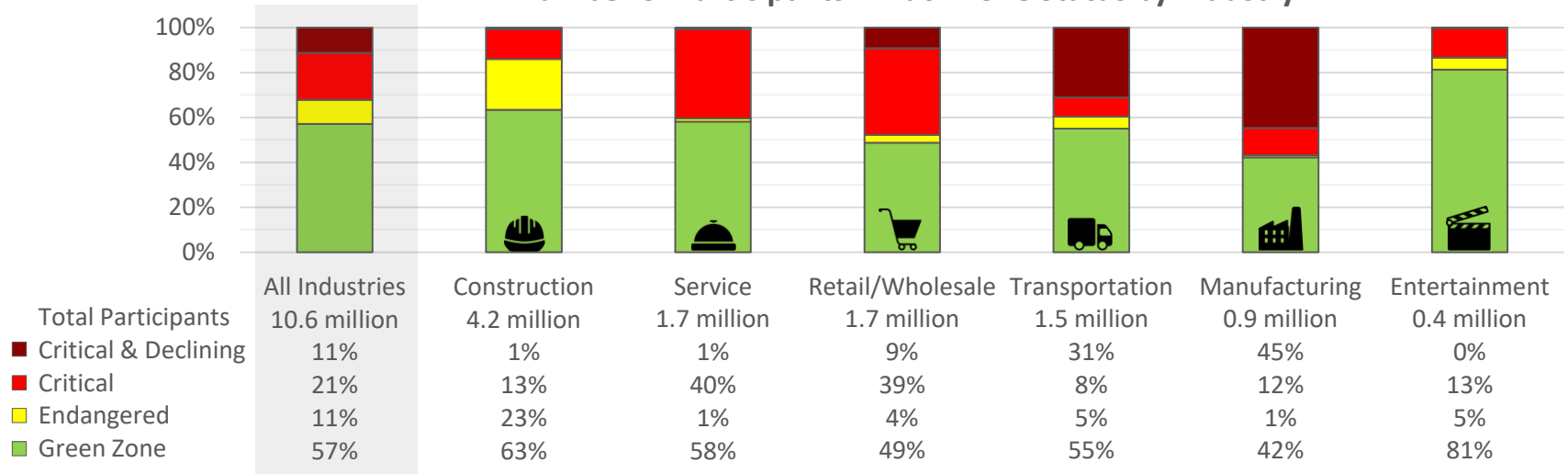
The Current Landscape

- Roughly 1,250 active multiemployer pension plans
 - Figure does not include over 100 plans already terminated or insolvent
 - Over 10 million active, inactive, and retired workers
- Close to 130 plans are in “critical and declining” status
 - Projected to exhaust their assets within the next 20 years
 - These plans cover over 1 million participants
- Other plans projected to fail beyond 20 years



Zone Status by Industry

Number of Participants in Each Zone Status by Industry

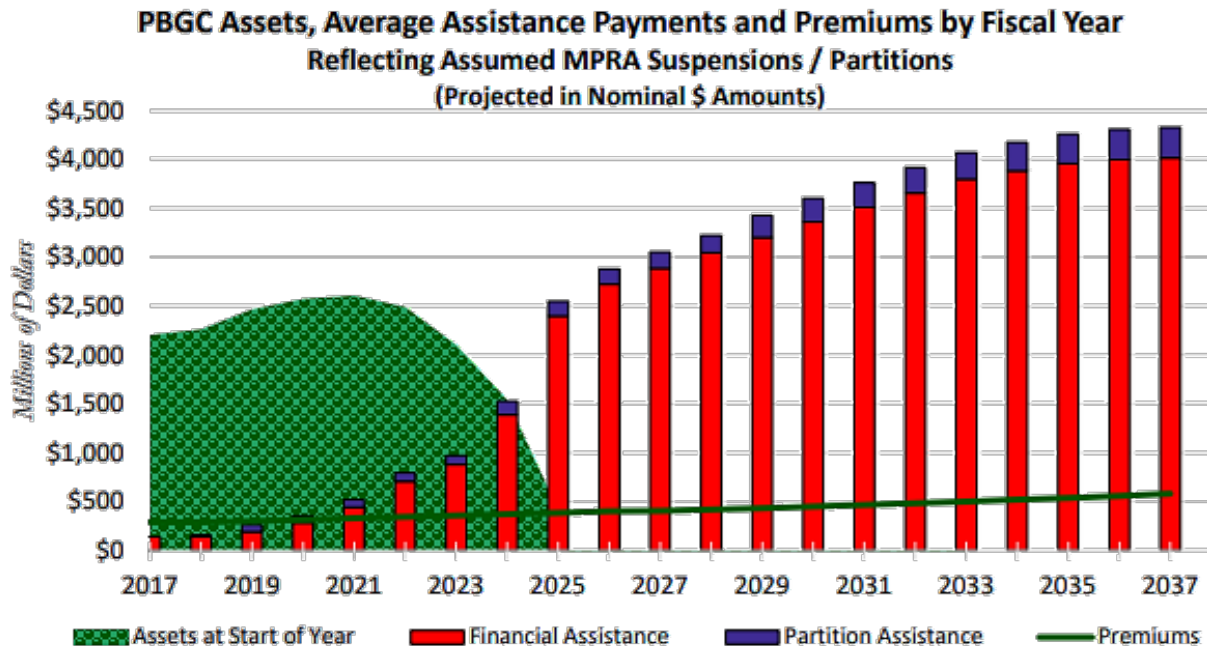


Source: Horizon Actuarial study of 2016 Form 5500 data

- Percentages may not sum to 100% due to rounding
- Approximately 0.2 million participants are covered in industries other than those shown in the chart above



PBGC Multiemployer Fund Projection



How The Current Situation Developed

Median Results for Multiemployer Pension Plans: 2002 to 2016

| Median Results <i>Based on Form 5500 Data</i> | Funded Percentages | | Annualized Returns | Average Contrib. Rate | Demographic Maturity Ratio | |
|--------------------------------------------------|--------------------|------|--------------------|-----------------------|----------------------------|------|
| | 2002 | 2016 | 2002-2016 | 2002-2016 | 2002 | 2016 |
| 2016 Zone Status | 2002 | 2016 | 2002-2016 | 2002-2016 | 2002 | 2016 |
| All Plans | 75% | 83% | 5.3% | x 2.6 | 1.0 | 1.7 |
| Critical & Declining | 76% | 52% | 5.3% | x 2.9 | 1.7 | 6.4 |
| Critical | 73% | 66% | 5.2% | x 2.9 | 1.0 | 2.0 |
| Endangered | 68% | 71% | 5.1% | x 2.7 | 1.0 | 1.6 |
| Green Zone | 77% | 90% | 5.4% | x 2.4 | 0.8 | 1.4 |

- Source: Horizon Actuarial study of Form 5500 data.
- Conclusions supported by 2018 study of Form 5500 data by Segal Consulting.
See pages 21-34: <https://nccmp.org/wp-content/uploads/2018/09/Appropriateness-of-Current-Assumptions.pdf>



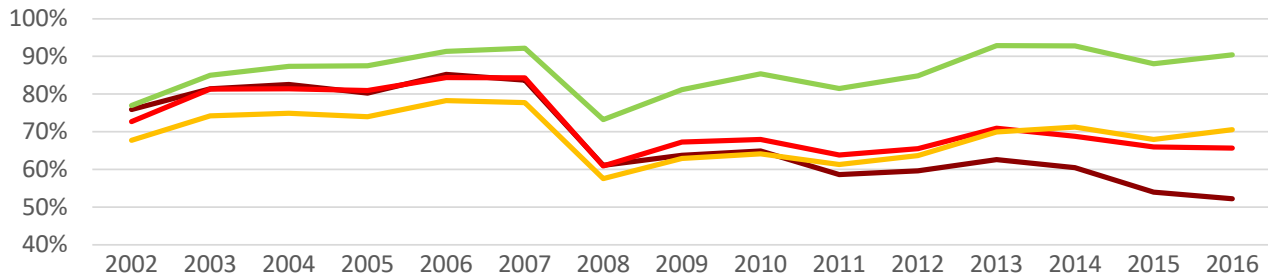
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Funded Percentage vs. Maturity

Median Market Value Funded Percentages (End of Year)

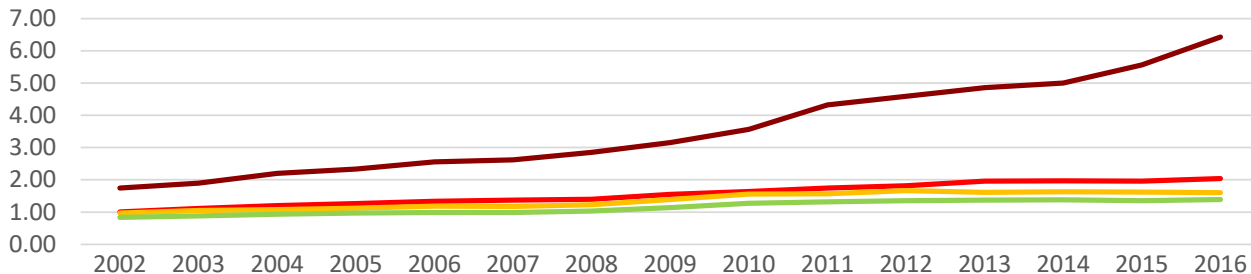


- Critical & Declining
- Critical
- Endangered
- Green Zone

Source: Horizon Actuarial study of Form 5500 data

- Funded percentages include calendar year plans only and are measured as of December 31 based on market value of assets and unit credit accrued liability
- Participant ratio represents the number of inactive and retired participants over the number of active participants
- Zone status determined based on 2016 Form 5500

Median Participant Ratios: Inactive to Active (End of Plan Year)



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Plan Governance



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Plan Governance

- Trustee ability to improve benefits
 - Funding level
 - Use of investment gains
- Benefit accrual limitations
- Asset allocation
 - Plan maturity
 - Benefit design
- Disclosures and transparency



Funding Rules

For more a history of multiemployer funding rules, please refer to materials from Session 1.

https://www.actuary.org/sites/default/files/2019-07/MEP_Hill_Briefing_Session1.pdf



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Multiemployer Funding Basics

- Plan assets
 - ▣ Fair market value, or
 - ▣ Actuarial (smoothed) value
- Plan liabilities
 - ▣ Present value of benefits already accrued
 - ▣ Based on discount rate and other actuarial assumptions
- Funded status
 - ▣ Unfunded liability = plan liabilities in excess of plan assets
 - ▣ Funded percentage = plan assets / plan liabilities



Funding Standard Account

- First implemented as part of ERISA in 1976
- Notional account used to determine minimum funding requirements
- Annual plan costs
 - Normal cost
 - Benefits earned in plan year plus administrative expenses
 - Amortizations of changes in unfunded liability
- “Credit balance” = cumulative contributions exceed costs
- “Funding deficiency” = cumulative costs exceed contributions

*“ERISA” = Employee Retirement
Income Security Act of 1974*



Multiemployer “Zone Status”

| Zone Status | General Tests |
|-------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Green Zone | <ul style="list-style-type: none">- Current funded percentage at least 80%, <u>and</u>- No projected funding deficiency in next 7 years |
| Endangered | <ul style="list-style-type: none">- Current funded percentage below 80%, <u>or</u>- Projected funding deficiency in next 7 years |
| Critical | <ul style="list-style-type: none">- Projected funding deficiency in next 4-5 years (initial tests)- Emerge from critical status if no funding deficiencies in 10 years |
| Critical and Declining | <ul style="list-style-type: none">- Projected funding deficiency in next 4-5 years, <u>and</u>- Projected insolvency in next 20 years (15 years in some cases) |

Defined in Pension Protection Act of 2006, amended by Multiemployer Pension Reform Act of 2014.

Above tests are simplified; special rules apply in certain situations.



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Zone Status Requirements

- **Green Zone** = no restrictions
- Endangered and critical plans must take corrective action
 - ▣ Designed to meet funding targets, usually over 10 years
 - ▣ Schedules of revised contributions and benefits
 - ▣ Union and employers adopt schedules through bargaining
- **Endangered** = funding improvement plan
 - ▣ Focus on future benefit accruals and contribution rates
- **Critical** = rehabilitation plan
 - ▣ May change future benefit accruals and contribution rates
 - ▣ May reduce “adjustable benefits” (e.g., early retirement, ancillary)
 - ▣ May declare exhaustion of reasonable measures



Tools Under MPRA

- For plans in **critical and declining** status only, first came about in 2015
 - ▣ Suspension of benefits
 - ▣ Partition of benefits (liability removal) by PBGC
 - ▣ Facilitated merger by PBGC

- Must enable plans to achieve projected insolvency
 - ▣ Otherwise, plan remains on path toward insolvency

- Plans must apply to federal agencies for approval
 - ▣ Significant plan resources to apply
 - ▣ Outcome of application uncertain
 - ▣ PBGC resources are very limited

“MPRA” = Multiemployer Pension Reform Act of 2014



Funding Rules: Looking Ahead

- Projected funded percentage is important
 - ▣ Current funded percentage doesn't tell where the plan is headed
 - ▣ Funding standard account is a lagging indicator
- Fundamental questions
 - ▣ When is a plan restricted from spending its surplus?
 - ▣ When must a plan take corrective action?
 - ▣ When must a plan restructure to remain solvent?
 - ▣ When is a plan deemed to fail?



Actuarial Assumptions

- General requirement
 - Each assumption must be individually reasonable
 - In aggregate, must be reasonable and represent actuary's best estimate
- Investment returns
 - Discount rate for determining plan liabilities
 - Expected investment return for projecting plan assets
- Future contributions
 - Based on input from the plan sponsor, acting reasonably and in good faith
 - Includes future covered employment levels (“industry activity”)
 - Also includes future contribution rates



Benefit Design



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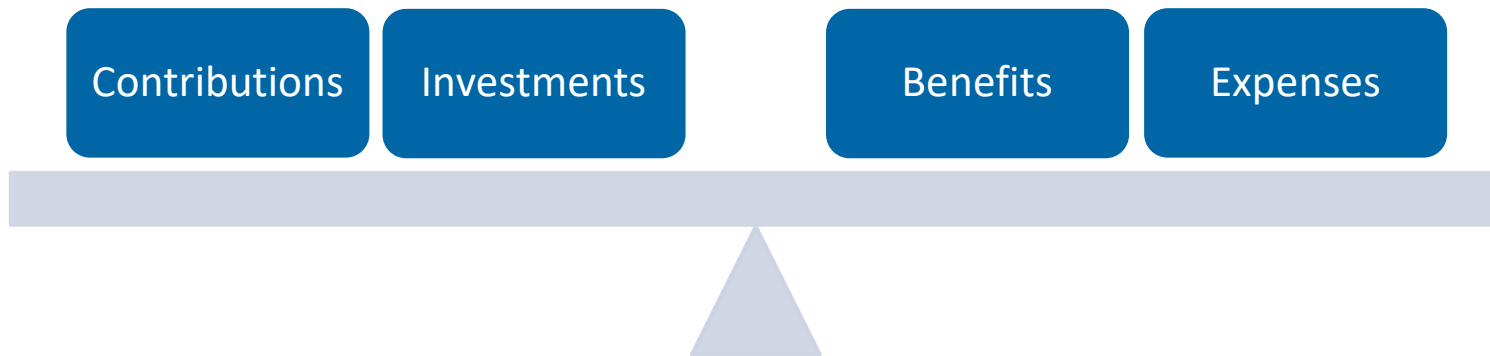
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Benefit Design: Fundamental Equation

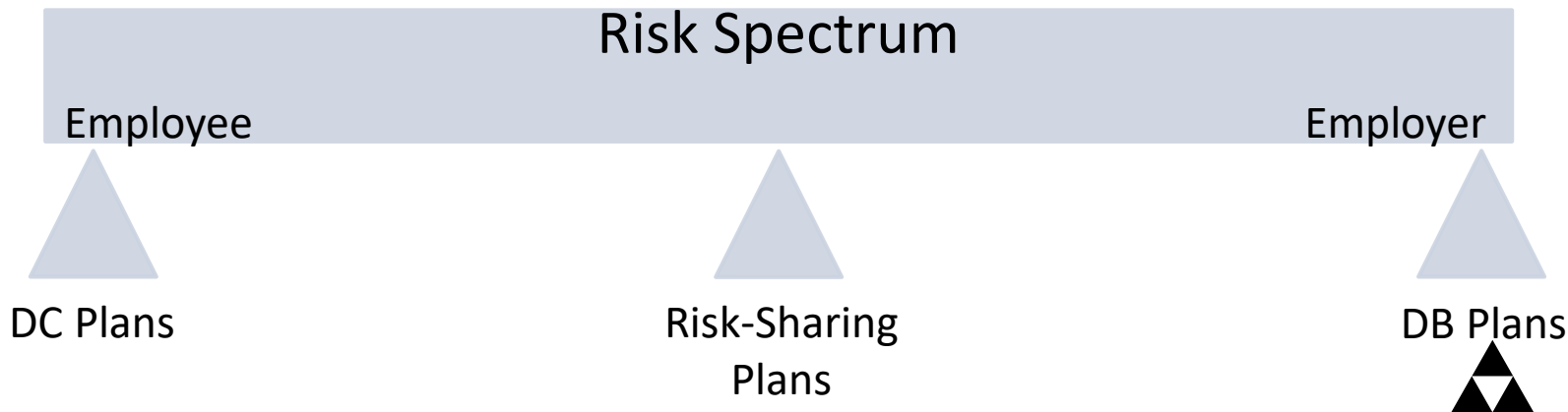
$$C + I = B + E$$

Contributions (C) + Investments (I) = Benefits (B) + Expenses (E)



Benefit Design

- DC is 100% risk to the employee
- DB traditionally viewed as 100% risk to the employer, but that has shifted in recent years
- Support for risk-sharing benefit designs.



Benefit Design: Plan Stability

- Current system
 - “Guaranteed” benefit obligations
 - Expected investment returns
- Mismatch contributes to instability
- Possible approaches
 - Funding approach with greater certainty
 - Benefit design with greater variability
- Balance between adequacy/cost and predictability



Benefit Design: Risk Sharing Plans

- Variable plans, adjustable plans, composite plans
 - Plans have mechanisms to adjust benefits (either automatically or based on trustee decisions) to maintain the funded status of the plan
- Maintain at or near 100% funded
- Reduce or eliminate withdrawal liability
- Reduce or eliminate the need for PBGC guarantees



Withdrawal Liability

For more information on Withdrawal Liability, please refer to materials from Session 1.

https://www.actuary.org/sites/default/files/2019-07/MEP_Hill_Briefing_Session1.pdf



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Withdrawal Liability: Overview

- Represents employer's share of UVB
 - "UVB" = Unfunded Vested Benefits
 - Shortfall of assets versus value of vested benefits
- UVB is based on
 - Allocation method selected by the Trustees, and
 - Assumptions selected by the Actuary
- Annual Payment
 - Based on historical work levels and contribution rate
 - Limited to 20 annual payments



Withdrawal Liability: Options

- Limited withdrawal liability in hybrid plans
 - UVB is managed in adjustable plans by design
 - No withdrawal liability in composite plans
- Allow protection for new employers
 - Two-pool methods exist, but still potential risk for new employers
 - Not available for construction industry plans



Withdrawal Liability: Options

- Adjust orphan liability
 - Liability removal (partition to PBGC)
 - Benefits are reduced
- PBGC authority to prescribe actuarial assumptions
 - Changes would need to be managed
 - Avoid unintended consequences



Withdrawal Liability: Options

- Adjust Annual Payment
 - Amount
 - Period
 - Limits
- Bankruptcy Rules
 - Often plans get cents on the dollar



Role of PBGC



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Role of PBGC

- Guarantee level
- Premium structure
 - Fixed dollar
 - Variable—based on funding level
 - Variable—based on investment risk
- Early intervention
- Relationship to benefit design



Academy Resources



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Academy Resources

- Reference materials can be found on the Academy's website
 - Presentations from all three briefings
 - Other materials on multiemployer pension plans
 - Link: <https://www.actuary.org/category/site-section/public-policy/pension>
- Contact Monica Konaté with questions and requests

Monica Konate

Pension Policy Analyst

konate@actuary.org



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Questions?

