DB PLANS

# A Christmas Gift For Multiemployer Plans

## The Multiemployer Pension Reform Act of 2014, enacted in December, included several surprises for those who work on multiemployer pension plans.

BY JAMES E. HOLLAND, JR.

T*was the weeks before Christmas, and all through the land,*
*Trustees were worried about multiemployer plans.*
*They wrung their hands, and shook heads to and fro,*
*PPA would expire; zone status would go!*
*Solutions proposed had fate yet unknown,*
*But the light was still on in the Capitol dome.*
*And late one night, in the budget so dear,*
*A multiemployer reform act appeared.*
*What's this?, said the trustees. What have we here?*
*A new law to read? An answer to prayer?*

With some help and inspiration from the works of Clement Clarke Moore and Dr. Seuss, the verse above approximately sets out the situation in December 2014, when Congress appended the Multiemployer Pension Reform Act of 2014 (MPRA) to the Consolidated and Further Continuing Appropriations Act, 2015 (Public Law 113-235).

The MPRA became law when it was signed by President Obama on Dec. 16, 2014. For most of the provisions, the effective date of the changes is plan years beginning on or after Jan. 1, 2015. The initial reaction to MPRA has been mixed with relief that something was done but surprise with respect to some of the provisions, one of which is especially controversial. This article will review the reasons for the anxiety leading up to the law and the main provisions. A knowledge of the specifics of the rules for multiemployer plans is helpful but not required.

## BACKGROUND

Until the passage of the Pension Protection Act of 2006 (PPA), the minimum funding requirements found in the Internal Revenue Code (IRC) and ERISA had much in common for single-employer plans (including, for this purpose, multiple-employer plans (MEPs)) and multiemployer plans.[1] Single-employer plans did have an additional requirement relating to current liability, which focused on the funding for accrued benefits and was not a trivial concern.[2] The operative law was found in IRC §412. PPA changed the rules dramatically starting in 2008.

For single-employer plans, the minimum funding requirements focused exclusively on the accrued benefits, and the rules are found in new IRC §430. For multiemployer plans, the focus remained on funding for projected benefits. The old rules for the most part continued to apply but were now found in new IRC §431, as §412 became more of a pointer. Single-employer plans had a new IRC §436 that restricted certain benefits and amendments; multiemployer plans had a new IRC §432, which will be the focus of the discussion below.

Section 432 introduced the concept of the "zone status" of a multiemployer plan, which must be certified by the plan's actuary within the first 90 days of the plan year based upon projections for that plan year and succeeding plan years (up to six depending on the test). The certification is made to the IRS and the plan sponsor (generally the board of trustees).

Under PPA, a plan could be certified as critical, endangered or neither. If a plan is certified as critical, then a "rehabilitation plan" must be developed so that the plan would emerge from critical status by the end of 10 (or a greater number of) years. However, if emergence from critical status is not reasonably achievable, then the rehabilitation plan needs to provide for reasonable measures to avoid or delay insolvency. If a plan was not critical, but was endangered, then a "funding improvement plan" was to be developed to reduce the underfunding for accrued benefits by 33% over a 10-year period (or 20% over a 15-year period if "seriously endangered").

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While there were alternative tests for each status,[3] a plan that is considered critical will not be endangered.[4] Many of the tests for critical and endangered status revolve around whether the plan is projected to have an accumulated funding deficiency for the plan year or a subsequent plan year, as does the test for emergence from critical status. Thus, for example, if a plan is projected to have an accumulated funding deficiency in two years, the plan fails the tests for both critical status and endangered status, but will be considered critical. Accordingly, as a practical matter, an actuary would test first for critical status, and then for endangered status.

In part because of this ordering, the statuses became associated with the colors of a stoplight: a critical plan is in the "red zone," an endangered plan is in the "yellow zone," and a plan that is neither critical nor endangered is in the "green zone," or "safe zone."[5] If a plan is certified as "red" or "yellow," the plan sponsor must notify participants and beneficiaries, the bargaining parties, the Pension Benefit Guaranty Corporation (PBGC) and the Department of Labor (DOL).[6]

Plans that are critical have an exemption from the excise taxes under IRC §4971 for failure to satisfy the minimum funding standards. Importantly, plans that are critical may also reduce certain "adjustable benefits" under §432(e)(8) without causing a violation of the anti-cutback rule of §411(d)(6).

Adjustable benefits include certain early retirement benefits and retirement-type subsidies. Reductions in adjustable benefits require notice to participants, and do not impact those in pay status before notice is given. Accrued benefits payable at normal retirement age cannot be reduced under IRC §432(e)(8).

## SUNSET LOOMING

Under PPA, the provisions of IRC §432 were to expire for plan years beginning after Dec. 31, 2014, although plans operating under a rehabilitation plan or a funding improvement plan were to continue to do so, and the relevant provisions relating to the operation of such plans continued to apply.[7] Trustees, attorneys and actuaries were

1 Multiemployer plans under IRC §414(f), which includes a requirement that they are collectively bargained.
2 Current liability was part of the full funding limitation for all plans under IRC §412(c)(7).
3 See IRC §432(b).
4 IRC §432(b)(1) provides that a multiemployer plan is in endangered status if "… the plan is not in critical status …".
5 Many refer to a plan that is "seriously endangered" as being in the "orange zone."
6 The DOL discloses the notifications of red or yellow status on its website.
7 See PPA §221(c).

uncertain as to how the expiration date provisions would apply. For example, would a plan in the red zone continue to be exempt from the excise tax otherwise imposed upon the accumulated funding deficiency? Could a plan in the yellow zone become red?

What did appear certain was that a plan that was green in 2014 could not become red or yellow in a subsequent year, with the loss of any protection from excise taxes that would apply to any future funding deficiencies.

Aside from the looming expiration date, practitioners had identified a number of technical fixes they thought were needed to the multiemployer rules. Furthermore, the state of some plans had deteriorated to the point that insolvency (*i.e.,* the inability to pay benefits when due) was projected in the not too distant future.

Spurred by concerns about the expiration of the zone status provisions and the current state of some plans, the National Coordinating Commission for Multiemployer Plans (NCCMP) convened a Retirement Security Review Commission to make recommendations for changes in the law. The report, *Solutions Not Bailouts*, contained recommendations for a number of technical changes in the law but included a proposal to allow a deeply troubled plan to reduce accrued benefits, including those in pay status. The proposal to reduce benefits quickly became controversial.

In addition, the PBGC noted in its FY 2013 Projections Report (released in June 2014) that multiemployer plans covering about 1.5 million people are severely underfunded. That same report also stated that the multiemployer guarantee fund was projected to have a high likelihood of running out of money over the next 10 years.[8]

"The MPRA represents a sea change in the treatment of multiemployer plans."

## THE MULTIEMPLOYER PENSION REFORM ACT OF 2014

During most of 2014, the various stakeholders recognized the issues and the concerns with respect to multiemployer plans. Most accepted many of the technical changes suggested in *Solutions Not Bailouts*. However, there appeared to be a lack of consensus about the proposal to reduce benefits. It was December and no bill had been proposed with respect to any changes in the law, and there was talk that the 2014 expiration date might simply be extended a year or two. Congress was engaged in a lame duck session prior to the Republican party taking control of both chambers with the new Congress in 2015. The key bill to pass was a budget bill to keep the federal government running. There seemed to be no time for multiemployer plan issues.

Then, on or about Dec. 9, 2014, Reps. John Kline (R-Minn.) and George Miller (D-Cal.) proposed an addition to the budget bill. Division O was entitled "Multiemployer Pension Reform" and contained the MPRA. This was the first legislative language released concerning any changes to IRC §432. With no time for comment or debate, MPRA became law. In the month that has followed at the time this article was written in January 2015, trustees, attorneys and actuaries have been studying the law and its impact.

The key changes to the law made by the MPRA are:

1. Permanent repeal of the PPA sunset.
2. An increase in PBGC premiums for multiemployer plans from $13 per participant to $26 starting in 2015 (with indexing thereafter).
3. Permission for a plan that is not in critical status (red zone), but that is projected to be in critical status in any of the next five plan years, to elect to be in critical status starting in the current year.
4. Provide that a plan that would otherwise be in endangered status (yellow zone) but would not require any changes to emerge from endangered status would not be classified as yellow (endangered) but, rather to be "safe" (green).
5. Add new provisions that apply to deeply troubled plans that are in "critical and declining status" including a permitted reduction in accrued benefits.

The MPRA made other changes in the law, including:

- Closing the "revolving door" when dealing with critical status plans.[9]
- Repealing the reorganization provisions of the Internal Revenue Code[10] and ERISA (but keep the insolvency provisions[11] with modifications to fit with the zone status provisions).
- Disregarding certain contribution increases for withdrawal liability purposes.[12]

8 PBGC does not actually take over insolvent multiemployer plans, but provides financial assistance (in effect, a loan that may never be repaid) up to a limit of 100% of the first $11 plus 75% of the next $33 of the monthly accrued benefit per year of service. The maximum guaranty for a person with 30 years of service, for example, is thus less than $13,000, which is much less than the single-employer plan guaranty.

9 This provision has to do with the fact that the PPA provisions allowed a plan to emerge from critical status only to go immediately back into the red zone due to the treatment of amortization extensions.

10 IRC §§418–418D.

11 IRC §418E.

12 This may prove to be an important change the implications of which have not yet been considered in detail.

- Amending ERISA to allow the PBGC to facilitate mergers.
- Revising the provision under ERISA under which the PBGC can order the partition of a plan to apply to an "eligible multiemployer plan" and add additional requirements.[13]
- Expanding the required disclosures of plan information under ERISA §101(k).
- Making changes to the annual funding notice.

The increase in PBGC premiums was a shock to many (it was not a recommendation in *Solutions Not Bailouts*), but was predictable given the state of the PBGC's multiemployer fund. The changes to the zone status requirements will impact certifications due at the end of March 2015. Fig. 1 shows the differences before and after MPRA.

Actuaries will have to distinguish between more variations. A plan that is "olive" will still require notification to the PBGC even though the plan is not considered endangered. Plans that are critical and declining (dark red) are a special category, as discussed below.

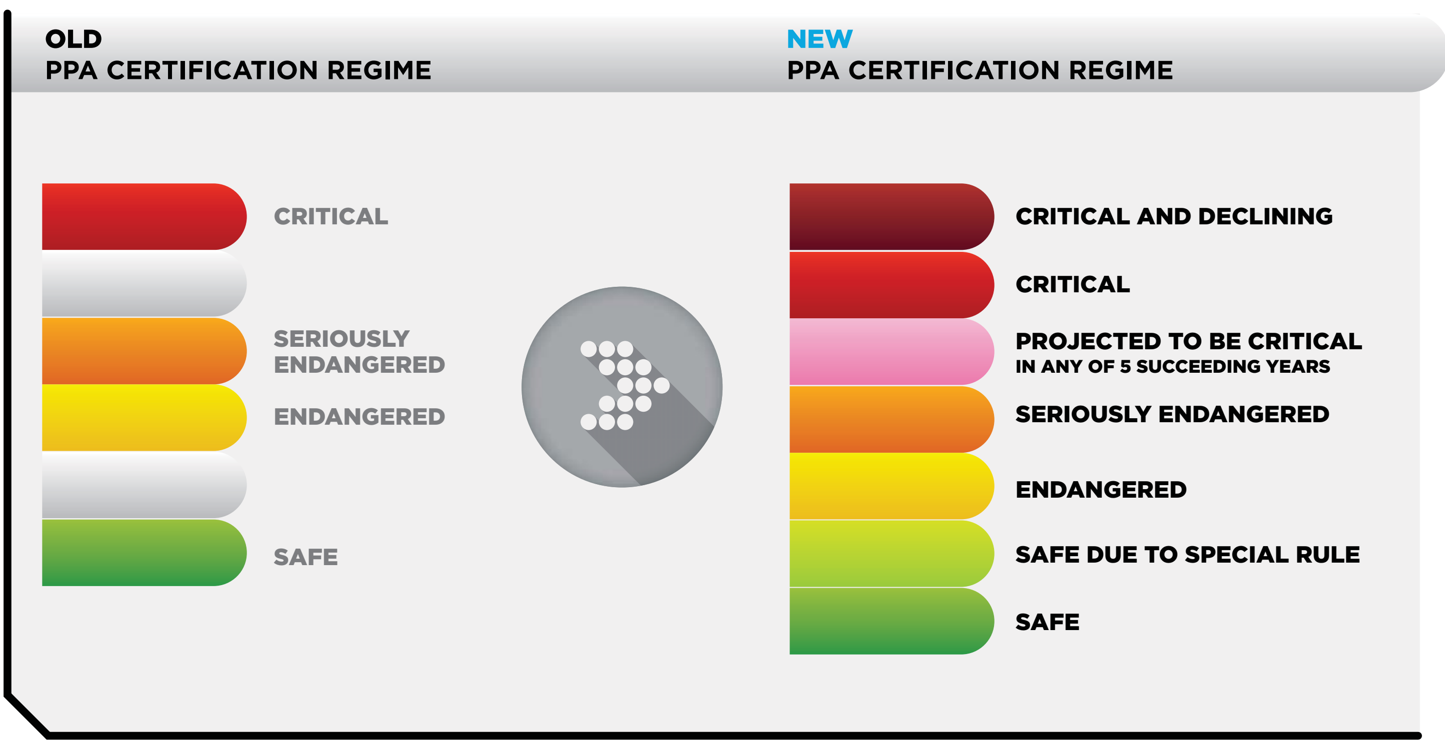
### REDUCTIONS IN ACCRUED BENEFITS

The most controversial aspect of MPRA is easily the provision (in new IRC §432(e)(9)) that permits a plan in critical and declining status (dark red) to reduce accrued benefits without violating IRC §411(d)(6).[14] The actual provision is quite different from what was put forth in *Solutions Not Bailouts*. First, a plan must be certified as dark red, which includes a certification that the plan will be insolvent within the meaning of IRC §418E in the current year or the next 14 years (or the next 19 years if the ratio of inactive to actives exceeds 2 to 1, or if the funded ratio is below 80%).

Second, the benefits that can be reduced and the process are much different than contemplated in *Solutions Not Bailouts*. Highlights of the MPRA requirements to reduce accrued benefits are:

- Application must be made to the IRS.[15]

## FIG. 1: MPRA, BEFORE AND AFTER




13 An eligible plan has to be one that is "critical and declining" (dark red), but there are some requirements that need to be satisfied for a partition that may make it less usable than some have thought.
14 The law uses the term "suspension" (perhaps because the reduction may be temporary), however, it is likely that any reduction will be permanent.
15 Originally, it was contemplated that application would be made to the PBGC.

> "The reduction in accrued benefits will not be an easy decision for plan sponsors seeking to balance the current participants' needs and expectations with long-term sustainability for all."

- Benefits for those participants who retired on disability or who are age 80 or older cannot be reduced and there is a phase-out of the reduction for those between 75 and 80 years of age.
- The benefits cannot be reduced below 110% of the amount that PBGC would guarantee (necessitating records for all potential impacted participants to see how much is guaranteed).
- If a plan has 10,000 or more participants, a retiree representative must be appointed to advocate for retirees, beneficiaries and terminated vested participants[16] throughout the process, and who can have actuarial and legal support paid for by the plan.
- A provision stating that, "Any suspension of benefits shall be equitably distributed across the participant and beneficiary population, taking into account factors," which includes a list of such factors.
- Notice requirements including publication in the *Federal Register* of the request to the IRS and the ability to comment.
- Consultation by the IRS with the PBGC and DOL.
- A 225-day period for the IRS to disapprove the request (with deemed approval if missed).
- A vote of participants to accept or reject the proposed reduction, which is to be administered by the IRS.
- An apparent requirement for the IRS to overturn a "no" vote for "systemically important plans" (defined, in relevant part, as the present value of financial assistance by the PBGC exceeding $1 billion) but to, perhaps, require a modification.
- A requirement that the IRS publish guidance within 180 days.

The reduction in accrued benefits will require a long process. Even though allowed by law, this provision is still controversial. It would not be surprising if lawsuits result from any action to reduce benefits. In the months to come, we will see how this provision (and the rest of MPRA) plays out.

## SUMMARY

MPRA represents a sea change in the treatment of multiemployer plans. Trustees, attorneys and actuaries will need to act quickly to understand the changes. The reduction in accrued benefits will not be an easy decision for plan sponsors seeking to balance the current participants' needs and expectations with long-term sustainability for all. We can expect that there will be hostility from participants and beneficiaries to any proposed reductions in benefits. How this plays out may be the subject of a future article. PC

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16 It appears that this individual would not advocate for active participants.