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A BENEFIT SUSPENSION APPLICATION UNDER MPRA

by | **Michael Reilly**

Applying for a suspension under the Multiemployer Pension Reform Act (MPRA) is a lengthy and complicated process. This article describes the steps one pension fund went through to apply for benefit suspensions.

The financial status of most multiemployer pension plans has improved since the financial crisis of 2008-09 as investment returns improved and trustees took action to improve funding levels.

For the small subset of plans facing insolvency, applying for benefit suspensions under the Multiemployer Pension Reform Act of 2014 (MPRA) is the last and only hope for keeping the plan operating indefinitely for the benefit of its participants. Research showed that about 5.9% of multiemployer plans, or 72 plans, were in critical and declining status in 2015 just after the law's passage, while more than 63% of plans were in the "green zone."[1,2] In 2018, 60 plans issued notices that they were in critical and declining status, according to the Department of Labor (DOL).[3]

As of this writing, the Department of Treasury has approved 13 MPRA applications for benefit suspensions and denied five. Another three applications are under review.[4]

MPRA expanded the range of benefits that multiemployer plans could cut under the law. Plans heading toward insolvency could reduce any benefits that were previously protected under the Employee Retirement Income Security Act (ERISA), subject to various restrictions on benefit cuts as described under the new law:

- Benefits cannot be reduced for participants age 80 or older (those between ages 75 and 80 are partially protected).
- Benefits cannot be reduced for participants receiving a disability pension under the terms of the plan.
- Cuts cannot reduce the benefit to an amount that is lower than 110% of the benefit guaranteed by the Pension Benefit Guaranty Corporation (PBGC).

MPRA allowed plans whose funded status was too severe to be remedied by the newly allowed benefit cuts to *partition* or separate a portion of the plan to receive PBGC assistance. The remaining portion of the plan would be projected to avoid insolvency without PBGC assistance.

While MPRA benefit cuts can be very painful to participants, benefits would still be higher than if the plan became insolvent and was taken over by PBGC. Moreover, there is much uncertainty about what will happen if PBGC itself goes insolvent and how much of participant benefits would still be guaranteed, if any.

Any plan seeking benefit cuts under MPRA must submit an application to the U.S. Department of the Treasury (and also PBGC, for those seeking a partition). The application requirements are quite complex and can be time-consuming and frustrating (to say the least). They are even more of a challenge if the plan has a complicated benefit design. The following case study of the benefit suspension application process followed by the Ironworkers Local 16 pension fund illustrates the labyrinthian process of designing an MPRA benefit suspension approach, preparing an application and seeking Treasury approval.

A Case Study—Ironworkers Local 16 Pension Fund

Factors Contributing to Funded Status Decline and Efforts to Remedy (Pre-MPRA)

Like most other multiemployer plans, the Ironworkers Local 16 pension fund suffered a substantial loss on its investments in 2008. To make matters considerably worse, the plan's contribution base units sharply dropped by more than 50% in just the two years following 2008 and continued to fall. By 2017, the contribution base units had declined more than 65% from 2008. The steep decline was driven in part by the permanent closure of an industrial park in the plan's area of Baltimore, Maryland. This industrial park had been a source of a significant portion of the plan's contributory hours for many years.

In addition, overall unemployment was rather high in the years following the 2008 market crash. But even as the rate of unemployment gradually came down, the plan struggled to recoup the contributory hours that had been lost. First, the union struggled to win new projects in the Baltimore area because of competing bids from nonunion contractors. Second, active Ironworkers were deterred from joining the Local 16 pension fund because of the rehabilitation plan that had been put in place to shore up the plan's financial status, which included lower accrual rates and higher contribution rates. The Local 16 pension fund was losing younger active Ironworkers—the financial lifeblood of a pension plan—to other locals. All of this meant that the contribution base units for the Local 16 pension fund would not rebound to pre-2008 levels.

The significantly lower level of contributory hours simply could not sustain the plan's existing benefit structure. As part of the plan's critical zone status rehabilitation plan to shore up the plan's financial status, the plan made sharp reductions to its adjustable benefits and doubled the hourly contribution rates for active participants. Despite these efforts, the plan could not avoid insolvency over a 20-year projection period. As a result, the plan was certified to be in *critical and* *declining* status for the plan year beginning January 1, 2015. This new status meant the plan met the first criterion for being eligible for benefit suspensions under MPRA.

MPRA Benefit Suspensions Design Considerations

Following the certification of critical and declining status, the plan's actuary began discussing various options for implementing benefit suspensions with the trustees. This process was not straightforward and required many difficult decisions. The plan had a complicated benefit structure that included service-graded accrual rates, a 13th check, banking of hours, a special cohort of participants (known as *grandfathered participants*) who were eligible for special subsidized early retirement benefits, and a partial lump-sum cashout window that had been discontinued just a few years prior.

While the plan had serious funding problems, it was in better shape than a lot of other critical and declining plans. Its funded percentage as of the 2015 certification was just over 62%, and it was projected to become insolvent in 19 years (under the statute, insolvency must be projected to occur within 20 years in order to be considered critical and declining). This relatively stronger financial status meant that, unlike many other critical and declining plans that were worse off, benefits could not be cut to the maximum extent allowed under the law—to 110% of the PBGC-guaranteed benefit. This meant that the board of trustees, in collaboration with the plan actuary, had the difficult task of designing a benefit suspensions program from scratch and making tough decisions about how to cut back on the plan's layered and convoluted benefit structure.

Several key principles guided the development of the benefit suspensions for the Ironworkers Local 16 pension fund:

- Groups that are more vulnerable, such as the elderly and widows/widowers, should have lower benefit cuts than those who are less vulnerable.
- The 13th check is a nonessential benefit and should therefore be eliminated in full before any core monthly benefits are cut.
- Active participants should not have to shoulder as much burden because they had already absorbed significant cuts to adjustable benefits under the rehabilitation plan, which included the contribution rate doubling while the pension accrual rate was cut in half.
- Long-service active participants should be protected because they were loyal to Local 16, and a number of these participants continued working in covered employment even after becoming eligible for unreduced early retirement benefits.
- Those who previously cashed out part of their pension at retirement should not incur less of a cut to their overall benefit at retirement (which included the amount that was cashed out at retirement) than those who did not receive a cash out.
- In no cases should a participant's core monthly benefit be reduced by more than 50% as a result of the benefit suspensions.

One of the earlier decisions made by the trustees was to develop an age-related benefit suspensions formula. Similar to an early retirement reduction factor, the Local 16 benefit suspension was calculated as the product of (1) a reduction percentage and (2) the number of months by which the participant's age as of the suspension effective date preceded age 80. This formula naturally shifted burden away from older participants toward younger participants, who were seen as less vulnerable.

Another early decision was to set a lower reduction rate for survivors who were in pay status as of the suspension effective date. The reasoning behind this was that a survivor must rely on a single income rather than on two incomes, as when the plan participant was still alive. The reduction rate for survivors was set equal to half the reduction rate that applied to plan participants.

The trustees decided not to reduce the benefits of active participants because the active participants had already absorbed significant cutbacks and had to shoulder significant increases in contribution rates under the rehabilitation plan. Moreover, the pension fund was already facing challenges with attracting and retaining new ironworkers.

However, this design created concerns about fairness. If benefit suspensions applied only to inactive participants as of the suspension effective date, it could create cases in which one participant retired from active status on the suspension effective date and received a full reduction while another participant of approximately the same age and level of service could retire a month later and get no reduction whatsoever. Another concern was that participants would try to game the system and delay retirement to avoid benefit suspensions altogether. Such changes in participant behavior would undermine the effectiveness of the proposed benefit suspensions and would be difficult to model.

To address those concerns, anyone who retires or terminates covered employment within two years of the benefit suspension effective date is subject to a partial benefit suspension reduction. The full reduction is reduced by 4% for each month that the retirement or termination of covered employment was after the benefit suspension effective date. For this purpose, termination of covered employment meant incurring a one-year break in service or death (in which case, the reduction would be passed on to the survivor).

The plan had a small group of high-service actives known as *grandfathered participants*. This group had earned at least 25 years of service as of June 2012 and was entitled to special subsidized benefits under the existing plan document provisions as a reward for their loyalty to the union. The trustees had initially opted to extend this group protections from the benefit suspension but modified the approach during the second application, described later in this article.

The final design consideration also came later in the process. Participants who had retired between 2003 and 2012 had been offered partial lump-sum cashouts (certain eligibility restrictions applied). It was noted that such cashouts were detrimental to the plan, partly because they accelerated the drawdown of plan assets. Moreover, if benefit suspensions were applied only to the regular monthly benefit currently being received, then the group that took the cashouts would receive a smaller cut to the overall benefit earned in the plan as of the date of retirement compared with the group that did not take the cashouts. For these reasons, the benefit suspension formula was applied to both the benefit being received as of the suspension effective date and the amount of the benefit that had been cashed out at retirement.

An Iterative Process

Designing the benefit suspensions required a great deal of discussion with the trustees, weighing pros and cons and constantly revising and tweaking the actuarial modeling to reflect changes to the benefit suspension design.

The suspensions also needed to be refreshed to reflect the most recent cash flow projections, such as the asset return and the level of contribution base units (CBUs). When an MPRA application is submitted to Treasury, the actuarial projections and modeling must be based on the level of assets as of the end of the most recent quarter. In addition, CBUs and other external factors modeled in the cash flow projections will be heavily scrutinized by Treasury to ensure that they are reasonable and reflect most recently available data. These external factors, in turn, directly affected how high the benefit cuts would be for the Ironworkers Local 16 pension fund participants, because under MPRA, the benefit suspensions must meet the following criteria:

- Sufficient for the plan to avoid insolvency
- Not excessive. Under MPRA, this means that if the benefit suspensions were reduced by the larger of 5% of the suspensions or 2% of the pre-suspension benefits, then the plan would go insolvent. Said another way, the benefit suspensions must be "just enough" for the plan to avoid insolvency. This second requirement, referred to as the *Goldilocks test*, leaves a very narrow margin within which the level of benefit suspensions must fall.

First Application to U.S. Treasury

After spending the better part of 2015 developing the benefit suspensions program, the application was prepped for a March 2016 submission. Revenue Procedure 2015-34 (later replaced by Revenue Procedure 2017-43) outlined all of the materials that must be submitted with the application. These materials totaled hundreds of pages for the Ironworkers Local 16 Pension Plan.

The plan received the first followup from PBGC roughly three months later. PBGC requested a comprehensive data set that included all of the data fields that were used in the calculation of actuarial liability and projected benefit payments. A few weeks later, PBGC requested detailed model output for more than a dozen participants. In requesting these "test lives," PBGC was attempting to verify that the model was set up appropriately and that it accurately implemented the proposed suspensions with federal limitations. After receiving the test lives information, PBGC asked a number of highly technical questions regarding the intended suspension design as well as various model inputs. Such questions were commonly paired with a request for detailed model output for additional test lives. In a few cases, PBGC asked the actuary to tweak the model to incorporate greater precision where simplifying assumptions and/or approaches had been used. Such back and forth with the PBGC went on for roughly three months. It was not uncommon for PBGC to set up a conference call with the actuary to clarify its requests, and some of the inquiries were resolved over the phone.

takeaways

- The Multiemployer Pension Reform Act (MPRA) was passed in 2014 and expands the range of benefits that multiemployer plans can cut.
- As of this writing, the Department of Treasury has approved 13 MPRA applications for benefit suspensions and denied five. Another three applications are under review.
- The Ironworkers Local 16 pension fund first applied for a benefit suspension under MPRA in 2015 after suffering a substantial loss on its investments in 2008 and experiencing a sharp decline in contributory hours.
- Designing the benefit suspensions required lengthy discussions with trustees and was an iterative process.
- The fund's first application was denied in 2016, and a second application was approved in 2018. Suspensions took effect October 1, 2018.

Shortly after PBGC made its initial request for additional information, Treasury did the same. While the PBGC inquiries were more focused on technical nuances within the data and in the actuarial modeling, the questions from Treasury focused mostly on justifying assumptions. Treasury took the position that the mortality and future contributory hours assumptions were not reasonable.

Treasury argued that the Ironworkers Local 16 pension fund mortality experience was not credible enough to use anything other than a current standardized table with generational mortality improvement and that the 1983 Group Annuity Mortality (GAM) mortality table that had been in use was unreasonable because it was dated.[5, 6] The actuary countered that the plan's gain/loss experience in the nearly ten years prior to the application provided no indication that the mortality assumption was a bad fit for the plan's demographics. The actuary also pointed to a recent study that showed that mortality rates were highest (by a significant margin) for Ironworkers compared to all other multiemployer construction industry participants that were surveyed. Treasury was not persuaded.

Regarding the future contributory hours assumption, Treasury took the position that it was not reasonable to assume that the level of CBUs would be the same in every year of the projection period because they had been decreasing in each of the three years preceding the MPRA application. The actuary and plan trustees countered that the assumed hours for the initial year in the projection period were 20% lower than the actual hours reported in the prior year and that there was an expectation, based on a number of important projects in the pipeline, that the plan's hours would stabilize. Like the counterpoints on the mortality assumption, Treasury was not persuaded. Moreover, when pressed for what would constitute a reasonable hours assumption, Treasury would not say.

In a conference call several weeks before the statutory deadline for issuing a final decision on the MPRA application, the representatives from Treasury stated that they would recommend denying the application on the basis of unreasonable assumptions. After discussing the benefits and drawbacks of withdrawing the application versus receiving a denial, the trustees decided to let Treasury deny the application. There were concerns that withdrawing the application would be perceived by plan participants as a sign that the application had been botched in some way. A withdrawal also is not as transparent as a denial. Treasury issues a formal letter detailing the reasons for denial and makes that letter available to the public.

In November 2016, a few days prior to the statutory deadline for issuing a final decision on the application, the application was formally denied during a conference call with a special master at Treasury. Treasury released its formal decision letter to the public later that day.

Second Application to U.S. Treasury

The process for preparing the second application to Treasury was similar to that of the first application. The proposed suspension cuts were 25% higher than those in the original proposal because the plan had lost ground by paying out roughly a year's worth of higher benefits. Higher cuts were now required to save the plan from insolvency.

Final regulations had also been released since the first application was submitted. Among other things, there was a new requirement for an attachment to the application with detailed justification for all of the assumptions. This amounted to an extra 20 pages of work, but it circumvented some of the back and forth with Treasury.

The second application was initially submitted in November 2017. Treasury requested a conference call within the initial two-day review period that Trea-

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sury had to confirm completeness. One of the exhibits was missing, and Treasury officials cautioned about two items in the application. First, they indicated their concern about the fixed 7% investment return assumption and stated a *select and ultimate assumption* (where the assumed asset return in the short term is lower than in the long term) may be more appropriate for a plan in financial distress.

The second concern was that the protections extended to grandfathered participants may violate the equitable distribution of benefit cuts provision laid out in the statute. Neither of these concerns was raised in the first application, and Treasury was careful to note that these concerns did not mean that the application would ultimately be rejected. However, there was a strong implication that such concerns would ultimately result in a denial.

For this reason, the trustees decided to change the investment return assumption to select and ultimate and to remove the protections being offered to the grandfathered participants.

The review process was very similar to that of the first application. Like the first application, PBGC requested a few refinements to the actuarial modeling to add greater precision.

None of these refinements had a material effect on either the actuarial liabilities or the cash flow projections. In one such case, the effect of the model tweak amounted to less than $1,000 on an accrued liability of more than $100 million. Unlike the first application, Treasury provided little comment during this time.

In early August 2018, Treasury approved the application. As required by law, a participant vote took place in September 2018, and the voting results were formally certified later in that same month. The suspensions took effect on October 1, 2018.

Conclusion

For plans that are facing insolvency, MPRA benefit suspensions can be the last and best hope for keeping the plan in existence for the maximum sustainable benefit of its participants. Applying for benefit suspensions under MPRA is a lengthy and complicated process that requires careful planning as well as extensive communication and coordination with trustees, plan practitioners and the government. Numerous factors relating to the plan's benefit design, the stakeholders, external forces, and any issues that have led to or can lead to a denial of the application must be considered throughout the process.

Endnotes

1. *The Multiemployer Retirement Plan Landscape: A Ten-Year Look (2006-2015).* International Foundation of Employee Benefit Plans and Horizon Actuarial Services, LLC.
2. Under MPRA, a multiemployer plan is in critical and declining status if it is in critical status and is projected to be insolvent in the next 15 years. The period is 20 years if the plan funded percentage is less than 80% or if the ratio of inactive participants to active participants is greater than 2 to 1.
3. See www.dol.gov/agencies/ebsa/about-ebsa/our-activities/public-disclosure/2018-funding-status-notices#2018-c-and-d.
4. See www.pionline.com/article/20190205/ONLINE/190209901/two-more-multiemployer-plans-get-ok-to-reduce-benefits.
5. Treasury referred to Actuarial Standard of Practice Number 35 (ASOP 35) as a basis for concluding that the mortality assumption was unreasonable. Section 3.3.5 of ASOP 35 describes a reasonable actuarial assumption. Section 3.5.3 of ASOP 35 outlines the relevant factors that an actuary should consider when selecting a mortality assumption. The plan actuary maintains that the mortality assumption was in compliance with these sections of ASOP 35.
6. The plan actuary demonstrated in written communication to Treasury that the 1983 GAM mortality table did not produce materially different results from the RP-2000 mortality table, suggesting that the effects of mortality improvement over two decades on the plan's projected cash flows was negligible.