New Law Allows Cuts in Multiemployer Pensions

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MarketWatch Blog by Alicia H. Munnell

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While plans need an additional tool to survive, the new law may not be ready for prime time.

When the President signed the omnibus budget and spending bill on December 16, 2014, he also signed into law sweeping changes, through the Multiemployer Pension Reform Act of 2014, to private sector multiemployer plans. The most controversial proposal allows deeply troubled multiemployer plans to suspend – read "cut" – benefit payments to retirees and accrued benefits for participants. We are sympathetic to the notion that multiemployer plans headed for insolvency need an additional tool, but are deeply concerned about whether the current proposal is ready for prime time. We are particularly concerned that the regulatory agencies – Treasury, the Pension Benefit Guaranty Corporation (PBGC), and the Department of Labor (DOL) – do not have the individual plan data to analyze the impact of benefit cuts on the long-term financial health of the plan.

Multiemployer defined benefit plans, which are created by bargaining agreements between a labor union and two or more employers, cover about 10 million unionized participants. These plans expanded benefits during the stock market boom in the 1990s and then lost substantial assets in the wake of two financial crises after the turn of the century. In addition, many plans are in industries – such as construction – hurt by the prolonged recession and others – such as trucking – that face a shrinking pool of unionized workers.

The great majority of multiemployer plans have responded to the financial pressures by cutting future benefits for active workers and raising employer contribution rates, allowing them to navigate to relatively secure footing. A significant number of plans, however, could run out of money in the next 20 years. The PBGC, which guarantees pension benefits for insolvent plans, does not have the resources to solve the problem.

The Multiemployer Pension Reform Act of 2014 creates a new plan status known as "critical and declining status" for plans likely to become insolvent in the next 15 to 20 years. Plans in this status can apply to the Treasury to suspend benefits for retirees and reduce accrued benefits for active workers. The sponsor must show that it has taken all reasonable measures to forestall insolvency and that the proposed benefit suspension will ensure solvency. A participant's benefit cannot be reduced below 110 percent of the PBGC guarantee. Limitations are provided for those 75 and older, and those 80 and older are exempt. Suspensions must first be allocated to a participant's service for an employer that withdrew from the plan without paying its full withdrawal liability.

Procedurally, the plan sponsor applies to the Treasury for the right to suspend benefits, simultaneously notifying participants, beneficiaries, contributing employers, and the respective union representatives. If the Treasury approves, the suspension is subject to a vote of all participants and union representatives within 30 days. If the suspension is rejected, the

Treasury, in consultation with the PBGC and the DOL, must decide if the plan is “systemically important” – that is, whether it would increase PBGC’s projected liabilities by more than $1 billion. If so, the Treasury, again in consultation with the PBGC and the DOL, can override the negative vote.

We analyzed the impact of such a proposal for the Central States Teamsters plan, the plan for which the proposal was originally designed. Our analysis suggests that, using widely accepted preference parameters, overall welfare would be higher in a world where the accrued benefits of all participants were reduced in order to return the plan to solvency. However, these calculations highlight the sensitivity of the outcome to assumptions and shows that while achieving solvency, the plan would be operating at an extremely low level of funding.

The possibility of cutting accrued benefits violates the central anti-cutback provision of the Employee Retirement Income Security Act (ERISA) and could set a dangerous precedent. So, its applicability needs to be carefully circumscribed. Most importantly, the Treasury, the PBGC, and the DOL should have access to the detailed plan data underlying the actuarial plan reports, and perform stochastic modeling of returns to assure that the painful remedy would actually result in solvency. In short, while we agree that multiemployer plans need an additional tool to survive, we worry whether the current proposal is really ready for prime time.