Multi-Elert® **Volume 3 • Issue 1**
A Service of the NCCMP **May 19, 2003**

TOPIC: MULTIEMPLOYER PENSION PLAN FUNDING RELIEF

EXECUTIVE SUMMARY:

THREE CONSECUTIVE YEARS OF NEGATIVE INVESTMENT MARKET PERFORMANCE HAVE PLACED MANY MULTIEMPLOYER DEFINED BENEFIT PENSION PLANS IN JEOPARDY OF FAILING TO MEET THEIR MINIMUM FUNDING REQUIREMENTS. OVER THE PAST SEVERAL MONTHS, THE NCCMP HAS BEEN DEEPLY ENGAGED IN ASSESSING THE SCOPE AND MAGNITUDE OF THIS PROBLEM AND DEVELOPING PROPOSALS AND STRATEGIES FOR ENGAGING THE REGULATORY AND LEGISLATIVE PROCESSES. DRAWING ON THIS WORK, THE NCCMP HAS MOUNTED AN AGGRESSIVE CAMPAIGN ON BOTH FRONTS FOR RELIEF TO GAIN TIME FOR TRUSTEES AND BARGAINING PARTIES TO EVALUATE THEIR OWN PARTICULAR SITUATIONS AND ACT ACCORDINGLY.

ON FRIDAY, APRIL 11, A BI-PARTISAN BILL - H.R. 1776, *"THE PENSION PRESERVATION AND SAVINGS EXPANSION ACT OF 2003"* WAS INTRODUCED BY CONGRESSMEN ROB PORTMAN AND BENJAMIN CARDIN. THE BILL INCLUDES, AMONG OTHER THINGS, THE LEGISLATIVE RELIEF REQUESTED BY THE NCCMP (SEE SECTION 708). THIS ISSUE OF MULTI-ELERT DESCRIBES THE PROBLEM AND OUR PROPOSED REGULATORY AND LEGISLATIVE RELIEF AND ENCOURAGES PLAN TRUSTEES AND PROFESSIONAL ADVISORS TO TAKE ALL STEPS NECESSARY TO EVALUATE THE SHORT- AND LONG-TERM IMPLICATIONS FOR THEIR PLANS AND ACT ACCORDINGLY.

PURPOSE: TO ALERT TRUSTEES AND THEIR PROFESSIONAL ADVISORS OF POTENTIAL MINIMUM FUNDING PROBLEMS AND TO ENCOURAGE PROMPT ACTION BY PLAN FIDUCIARIES AND SETTLORS.

CATEGORY: INFORMATIONAL

ACTION: CONTACT YOUR CONGRESSIONAL REPRESENTATIVE AND ASK HIM OR HER TO SUPPORT SECTION 708 OF H.R. 1776

ISSUER: U.S. HOUSE OF REPRESENTATIVES

TARGET AUDIENCE: DEFINED BENEFIT PENSION PLAN TRUSTEES AND ADVISORS AND LEADERSHIP OF SPONSORING ORGANIZATIONS

FORWARD COMMENTS TO: *Multi-Elert@nccmp.org*

REFERENCE: VOL.3, ISSUE 1

SEE FOR MORE INFORMATION: ***THE PENSION PRESERVATION AND SAVINGS EXPANSION ACT OF 2003*** (H.R. 1776); IRC § 412(C)(11); ERISA § 302(C)(11)

NCCMP Launches a Coordinated Effort Seeking Funding Relief For Troubled Plans

Over the past three years, stories detailing the decline of the U. S. stock markets and the impact this decline has had on Americans' retirement plans have saturated the media. For the most part, these stories have concentrated on defined contribution plans, especially 401(k) plans, perhaps the best known of the defined contribution plans. During that time, participants in defined benefit plans have taken comfort from the fact that the investment risk is assumed by the plan rather than the individual participant.

For the most part, the effects of this market decline on defined benefit plans have not been the focus of much discussion. This is mainly because the actuarial methods commonly used for valuing assets smooth the more volatile year-to-year shifts in the market by spreading the recognition of investment gains and losses over a period of time (for example, 5 years). Nevertheless, defined benefit plans have also suffered significant losses, generally consistent with the overall decline in the stock markets. As this negative performance has continued, even the strongest of defined benefit plans are beginning to see its effect. What that means to our plans, and the activities of the NCCMP to address the problems created by this exceptional period in history are the subject of this issue of ***Multi-Elert***.

Background

Trustees and professional advisors to defined benefit pension plans are well aware that plan funding comes from a combination of contributions paid by contributing employers (usually based on hours worked) and from investment income on accumulated assets. They are also aware that income from all sources must fall within a range between the minimum required contribution, and a full funding limit above which contributing employers may be subject to excise taxes and be prevented from taking the full tax deduction for their contributions in the year in which they are made. For mature plans (like most of our plans) investment income makes up the majority of plan funding. For most of the time since the passage of ERISA in 1974, investment returns have consistently exceeded the assumed actuarial rates of return (typically 7% - 7.5%). The gains experienced by plans have pushed them to their funding limits. In fact, in recent years trustees of many plans have had to make benefit improvements so contributing employers could take the full current tax deductions for their contributions.

As noted above, however, investment returns for the last three consecutive years have been negative. This situation has few precedents, with this episode marking only the third time since the beginning of the 20th century and the first time since before World War II that equity markets have produced negative results for three consecutive years. Although most plans are still on track for funding their benefit obligations, this recent prolonged downturn in the markets could cause as many as a third or more of all multiemployer defined benefit plans to miss their technical minimum funding requirement in the near future. If this were to happen, trustees and the bargaining parties who sponsor such plans would be faced with serious decisions in order to bring plan costs and income into balance.

What is being done?

Since the middle of last year, the NCCMP has intensively studied this problem to determine how widespread it is and how severe the consequences might be for those affected. A bullet point summary of the NCCMP's activities, findings and the current status of this issue is provided below. These findings support the conclusions that: this issue represents a significant problem for multiemployer plans as a whole; it is widespread, both in terms of the industries affected and the size and locations of the plans; and without immediate relief, it poses the potential for sufficient long-term damage to all multiemployer defined benefit pension plans and to the bargaining relationships that enable them to exist. **It is also important to note, however, that not all plans will have a funding problem and that the proposals being pursued for troubled plans are intended as options for those plans rather than mandatory for all plans.**

The result of the NCCMP's analysis has been to develop a two-track strategy to gain regulatory relief to the extent possible from the IRS and to propose legislation that would allow our plans to amortize the investment losses suffered during this unusual "emergency" period over a 30 year period rather than the 15 year period permitted under the current rules. In combination, these proposals will resolve the potential funding crisis for some troubled plans. For those with the most severe problems, however, these changes will provide a little more time for the trustees and the bargaining parties to take whatever actions may be necessary to adjust contributions and benefit levels to preserve their plans, ideally with help from a recovering investment market.

In early April, representatives of the NCCMP met with IRS and PBGC officials to discuss technical proposals for regulatory relief. Additionally, on April 11, 2003, Ohio Congressman Rob Portman and Maryland Congressman Ben Cardin, along with nine co-sponsors introduced the bipartisan "Pension Preservation and Savings Expansion Act of 2003" which contains the provisions advocated by the NCCMP to provide the desired funding relief for multiemployer plans. Support for this bill comes from a full range of affiliated unions and employer associations in a variety of industries. The obvious and direct impact on our funds and their contributing employers has resulted in a broad coalition of support for these legislative and regulatory initiatives.

What can you do?

The first thing that you can do is to work with your boards of trustees and professional advisors to gain a full understanding of the impact the market decline has had on your particular fund or funds. The fund actuary should be asked to perform the necessary studies to determine whether and, if so, when and to what extent your fund may experience a funding deficiency. If your fund is expected to have a problem in the future, you can begin to formulate a plan to address your particular circumstances as soon as possible.

As obvious and logical as these proposals may appear to those who are involved with multiemployer plans, the fact is that this proposal is competing with proposals in Congress dealing with the President's proposals to eliminate taxes on dividends and stimulate the economy which makes an already difficult road that much more treacherous to navigate. **For these reasons, your assistance is essential in raising the awareness of your Congressional Representatives (especially those on the Ways and Means or Education and the Workforce Committees) and Senators of the importance of maintaining multiemployer defined benefit pension plans and the need for their support of the Pension Preservation and Savings Expansion Act of 2003, with particular emphasis on Section 708 of the Bill. One way to ensure that this message is clearly conveyed is to send a letter to your Congressman, similar to the attached sample letters, reinforcing from your standpoint why the requested relief is so desperately needed.**

HIGHLIGHTS OF NCCMP FUNDING RELIEF EFFORTS

- Mature pension plans (including most multiemployer plans) depend primarily on investment returns, rather than contribution income, for funding.
- Funding rules for multiemployer plans, as with all pension plans, were developed following the passage of ERISA in 1974.
- These rules did not anticipate the kind of prolonged periods of negative market performance we are currently experiencing.
- The period encompassing calendar years 2000, 2001 and 2002, mark the first time since the beginning of World War II, and only the third time since the beginning of the 20th century, that the equity markets have suffered three consecutive years of negative performance.
- NCCMP Affiliates have reported that they have plans that face imminent funding problems that will result in a violation of the minimum funding rules in the absence of some form of relief.
- Under the law, employers are obligated to fund plans at the minimum funding level, even if that would exceed the employers' obligation under the collective bargaining agreement.
- *These plans are not in danger of meeting their long-term benefit funding requirements, but will fail to meet the current technical funding requirements.*
- Nevertheless, ***trustees faced with this situation could be forced to assess contributing employers for additional contributions in order to meet the minimum funding obligations.***
- ***Unlike assessments for withdrawal liability that are only made when an employer withdraws from the fund or has no further obligation to contribute to it, these assessments would be levied against all contributing employers, including those who have steadfastly supported multiemployer defined benefit plans.***
- ***In addition to these contribution assessments, contributing employers could be hit with excise taxes based on the amount of the underfunding.***
- ***The magnitude of these additional assessments would at best further hinder contributing employers' ability to remain price competitive and, in the worst cases, could potentially bankrupt some employers.***
- Based on these reports, the NCCMP asked The Segal Company (which advises nearly 25% of all multiemployer defined benefit plans) to sample their client base to determine if these were isolated situations, or an indication of a widespread problem.
- The NCCMP simultaneously retained Gary Ford of the Groom Law Group as outside counsel for technical advice regarding possible regulatory and / or legislative relief. Mr. Ford's credentials for this assignment include having served as former ERISA Counsel to the Senate Committee on Labor and Human Resources and as former General Counsel to the PBGC.
- The Segal Company reviewed nearly 150 of its client funds for which it had recently completed actuarial valuations and identified over 40 plans that could fail to meet their technical minimum funding requirements in the near future without relief from the current rules.
- Segal's review showed that the problem is widespread (overall, over 75% of plans are projected to have a minimum funding problem at some point if all of the recent investment experience makes its way into the actuarial value of assets, absent a change to increase contributions or reduce benefits), and that these troubled plans are not limited to any particular industry, or size, but included a cross section of plans by industry, geographic area and size.

- Inquiries received by the NCCMP from other actuarial firms regarding this matter provide further evidence of the widespread scope of the problem.
- After careful analysis, it was determined that a two-pronged, regulatory and legislative approach would improve our chances of obtaining needed relief.
- A range of technical proposals were developed and tested that might be proposed to the IRS for regulatory relief.
- These technical proposals would postpone the point at which the plans would fall below the minimum required funding levels, to provide time for the bargaining parties to negotiate additional contributions and / or benefit design changes and for the markets to recover.
- A limited legislative proposal that would extend the amortization period from 15 to 30 years only for investment losses incurred during an isolated "Emergency" period (2000 – 2003), was determined to be most effective and would provide helpful relief for many such plans.
- A legislative strategy was developed in order to identify the legislation most likely to achieve passage this year.
- On April 7, representatives of the NCCMP met with officials of the IRS and PBGC to discuss potential regulatory relief, focusing on three main suggestions:
    - Obtaining blanket approval to switch to an asset valuation corridor that provides more flexibility to smooth the recognition of recent losses;
    - Obtaining automatic approval for multiemployer plans to use the shortfall funding method; and
    - Easing the availability of obtaining 5 year amortization extensions.
- On April 11, Representatives Rob Portman and Ben Cardin provided the second layer of proposed relief when they introduced the bi-partisan ***Pension Preservation and Savings Expansion Act of 2003***, Section 708 of which contains the multiemployer pension plan relief proposal advocated by the NCCMP.
- Since then, an ongoing educational campaign has been conducted to inform both labor and employer groups of the implications of this issue, which has met with consistent and strong support of continued, coordinated action by the NCCMP and all of its constituent groups.

THESE ACTIONS ARE BEING TAKEN BECAUSE OF THE POTENTIALLY DEVASTATING EFFECT THE IMPOSITION OF EXTRA-CONTRACTUAL CONTRIBUTION REQUIREMENTS MAY HAVE ON EMPLOYERS WHO CONTRIBUTE TO MULTIEMPLOYER PLANS. REGARDLESS OF THE INDUSTRY THAT FIRST EXPERIENCES THE PROBLEM, A HIGHLY VISIBLE COLLAPSE OF ONE OR TWO PLANS COULD CAUSE PANIC AMONG EMPLOYERS WHO DO NOT FULLY COMPREHEND THIS ISSUE -- ACROSS THE FULL SPECTUM OF INDUSTIES THAT SPONSOR MULTIEMPLOYER PLANS. THIS COULD JEOPARDIZE THE CONTINUED VIABILITY OF THE MULTIEMPLOYER PLAN SYSTEM BY TRIGGERING WIDESPREAD EMPLOYER WITHDRAWALS, LITIGATION BY PLAN TRUSTEES AGAINST PLAN SPONSORS AND DISRUPTION OF THE FUNDAMENTAL COLLECTIVE BARGAINING RELATIIONSHIPS THAT SUPPORT THEM.

It is also noteworthy that the American Academy of Actuaries has formed a committee of multiemployer actuaries to examine this issue, independent of the actions of the NCCMP. The conclusions of that group regarding the need for intervention in order to avoid funding deficiencies, as well as their proposals for regulatory relief, were quite similar to those developed by the NCCMP.

DRAFT PROTOTYPE LETTER FROM UNION OFFICIALS

May 14, 2003

[Democrat Ways and Means or Education and the Workforce Committee Member]

Re: Multiemployer Plan Emergency Investment Loss Proposal

Dear ____:

I am writing to ask for your help and support in passing Section 708 of H.R. 1776, the "Pension Preservation and Savings Expansion Act of 2003" the bipartisan pension reform bill recently introduced by Reps. Portman and Cardin. This provision is a critical one to unions like ours whose members are covered by multiemployer pension plans.

Multiemployer plans are maintained pursuant to collective bargaining agreements between unrelated employers – generally within the same industry – and unions. These plans provide employees with the opportunity to be covered by a defined benefit plan that gives them "portability" to earn continuous benefits as they go from job to job within the same industry. In our case, workers that we represent are covered by the _______ Funds, which are funded by contributions from [trucking companies, plumbing contractors, etc.] in the _______ area.

Multiemployer plans have a long history of sound, conservative funding and, unlike single employer plans, have never been a problem for the Pension Benefit Guaranty Corporation (PBGC). However, the almost unprecedented decline in the stock market over the last three and a half years has had a particularly adverse effect on many "mature" multiemployer plans. These plans, which have growing numbers of older and retired participants, depend greatly on investment returns to augment employer contributions. The impact of the stock markets' decline has been made worse for certain multiemployer plans because, in the 1990s, rising stock markets put pressure on plans to increase benefits or reduce contributions to avoid violating Internal Revenue Code deduction limits and triggering related excise taxes for contributing employers.

As a result, some multiemployer plans now face ominous near-term funding problems. Actuaries working with these plans report that approximately one-third of the plans could face funding deficiencies in the next several years. The companies that contribute to the _____ Funds in which our members participate could face significant excise tax penalties on funding deficiencies plus mandatory additional pension contributions – on top of the contributions agreed to through collective bargaining. Further, this could seriously disrupt labor relations if we must accept sharp cuts in benefits and wages in future bargaining in order to balance out skyrocketing pension contributions.

These plans have plenty of cash to pay benefits. If given the time, we can work with the employers and the plans' trustees to come up with sustainable, long-term solutions by adjusting future benefits and/or contributions. The alternative – drastic changes in benefits and contributions and harsh penalties on employers – could be catastrophic to plan participants.

Section 708 of H.R. 1776 would provide multiemployer plans with time to develop long-term solutions by permitting them to amortize investment losses incurred between July 1, 1999 and December 31, 2003 over 30 years instead of 15 years. This proposal is analogous to refinancing a mortgage. It would not excuse plans from paying promised benefits or in any way reduce the obligation of employers to fund them. It also would not reduce Treasury revenues. And because the PBGC's multiemployer pension guarantee program has a longstanding and growing surplus, this relief would not threaten the PBGC's financial condition.

We ask for your help and support in passing this very important provision [by co-sponsoring H.R. 1776 and/or by informing Chairman Thomas and Ranking Member Rangel/Chairman Boehner and Ranking Member Miller of the importance of this provision]. If you have any questions or need additional information, please contact ___________ at __________.

Thank you very much for your consideration.

Sincerely,

DRAFT PROTOTYPE LETTER FROM EMPLOYER REPRESENTATIVES

May 6, 2003

[Republican Ways and Means or Education and the Workforce Committee Member]

Re: Multiemployer Plan Emergency Investment Loss Proposal

Dear ____:

I am writing to ask for your help and support in passing section 708 of H.R. 1776, the pension reform bill recently introduced by Reps. Portman and Cardin. This provision is a critical one to companies like ours that contribute to multiemployer pension plans.

Multiemployer plans are maintained pursuant to collective bargaining agreements between unrelated employers – generally within the same industry – and unions. These plans provide small, medium and large employers with the opportunity to provide their employees with a defined benefit plan that gives them "portability" to earn continuous benefits as they go from job to job within the same industry. In our case, we and other _______ [trucking companies, plumbing contractors, etc.] in the _______ area contribute to the _________ Funds, which cover our _______ [name of unions] workers.

Multiemployer plans have a long history of sound, conservative funding and have never been a problem for the Pension Benefit Guaranty Corporation (PBGC). However, the almost unprecedented decline in the stock market over the last three and a half years has had a particularly adverse effect on many "mature" multiemployer plans. These plans, which have growing numbers of older and retired participants, depend greatly on investment returns to augment employer contributions. The impact of the stock markets' decline has been made worse for certain multiemployer plans because, in the 1990s, rising stock markets put pressure on plans to increase benefits or reduce contributions to avoid violating Internal Revenue Code deduction limits and triggering related excise taxes.

As a result, some multiemployer plans now face ominous near-term funding problems. Actuaries working with these plans report that approximately one-third of the plans could face funding deficiencies in the next several years. Our company and many others could face significant excise tax penalties on funding deficiencies plus mandatory additional pension contributions – on top of the contributions agreed to through collective bargaining.

These plans have plenty of cash to pay benefits. If given the time, we can come up with sustainable, long-term solutions by adjusting benefits and/or contributions. The alternative – drastic changes in benefits and contributions and harsh penalties on employers – could be catastrophic to both the plans and the industries that support them.

Section 708 of H.R. 1776 would provide multiemployer plans with time to develop long-term solutions by permitting them to amortize investment losses incurred between July 1999 and 2003 over 30 years instead of 15 years. This proposal is analogous to refinancing a mortgage. It would not excuse plans from paying promised benefits or in any way reduce the obligation of employers to fund them. It also would not reduce Treasury revenues. And because the PBGC's multiemployer pension guarantee program has a longstanding and growing surplus, this relief would not threaten the PBGC's financial condition.

We ask for your help and support in passing this very important provision [by co-sponsoring H.R. 1776 and/or by informing Chairman Thomas/Chairman Boehner of the importance of this provision]. If you have any questions or need additional information, please contact ___________ at __________.

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