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# ERISA Advisory

## Treasury, PBGC Begin to Wrestle with Multiemployer Pension Plan Reforms

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Late last year, Congress took drastic action to rescue the country's largest union-affiliated pension plans – and the government program that backstops them – from financial ruin. The Multiemployer Pension Reform Act of 2014 (MPRA), signed into law, on December 16, 2014, authorizes multiemployer pension plans (collectively bargained plans to which two or more unrelated employers contribute) to reduce benefits earned in the past if that is the only way to avoid running out of money. Plans that take this step may also be able to obtain immediate aid from the Pension Benefit Guaranty Corporation (PBGC), which previously subsidized plans could obtain only after they became insolvent.


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Questions and comments about the Steptoe ERISA Advisory are always welcome.

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### The Statutory Scheme

In broad outline, the new law allows a multiemployer plan to suspend the payment of accrued benefits, temporarily or permanently, if it is severely underfunded (in "critical condition," also known as being in the "red zone") and is projected to become insolvent within 14 years (19 years if its ratio of inactive to active participants is two-to-one or more). Suspensions require Treasury Department approval and can be vetoed by a vote of a majority of plan participants, although the veto can, in turn, be overridden by Treasury if the plan is "systemically important" (meaning, if its insolvency would cost the PBGC losses of more than $1 billion (indexed to the Social Security taxable wage base)).

MPRA imposes limits on the extent to which suspensions may reduce benefit payments:

- Accrued benefits may not be decreased below 110% of the level guaranteed by the PBGC, which is $11 per month times years of service under the plan plus 75% of the next $33 per month accrual, or a maximum of $35.75 per month times years of service. For example, if the plan benefit is $50 per month per year of credited service, a participant with 20 years of service would have an accrued benefit of $1,000 per month and a PBGC-guaranteed benefit of $715 per month. A benefit suspension could not reduce this entitlement to less than $786.50 per month.
- Starting at age 75, the permitted decrease is phased out, disappearing completely for participants 80 years of age or older. For instance, if the participant described above was 77 years old when the suspension went into effect, the cut in the participant's $1,000 a month pension would be limited to 60% of what would otherwise be permitted, so that the participant would continue to receive a monthly benefit of at least $871.90.
- Benefit suspension is entirely prohibited for participants who are receiving disability benefits.
- Suspensions may be different for different groups but must be spread "equitably." The statute lists a variety of factors to be taken into account in determining equity but is silent on how to apply them.

If a plan has suspended all of the benefits that it can and still is not projected to remain solvent, the next resort is "partition," which consists of spinning off a portion of its benefits to a separate plan for which the PBGC assumes financial, though not administrative, responsibility. The PBGC is not compelled to accept partitions. In fact, it may do so only if assuming the new burden does not jeopardize its ability to meet its other commitments. A partition has no impact on participants beyond the effect of the accompanying benefit suspensions. To a large extent, it is a legal fiction, almost wholly so during its first ten years, when PBGC premiums and withdrawal liability will be calculated without regard to the nominal split-up.

The new MPRA partition rules supersede the authority that the PBGC formerly had to partition a plan when a major contributing employer went into bankruptcy. That procedure, while potentially useful, was rarely used. The PBGC approved only about three partitions over a period of 35 years.

**Will MPRA Save Multiemployer Plans?**

No one knows how many plans will seek to use MPRA to suspend unsustainable benefits. The largest such plan, the Teamsters-affiliated Central States, Southeast, and Southwest Areas Pension Fund, with nearly 300,000 active and retired participants, has already announced that it will (and has even set up a website to provide information about the effort). Calculations by Boston College's Center for Retirement Research suggest that about 100 of the country's 1,400 multiemployer plans may be eligible for MPRA relief. Some of those may be in such hopeless condition that MPRA cannot save them. Others are very small and may seek to merge with bigger plans associated with the same union rather than cut benefits. (Another MPRA provision authorizes the PBGC to set up a program of financial and other assistance to facilitate mergers, though no details have been formulated yet.)

Since its enactment, MPRA has attracted sharp criticism, mitigated only by the critics' inability to devise any alternatives other than expending billions of tax dollars on a bailout (advocated by Democratic presidential hopeful Senator Bernie Sanders) or hoping that something will turn up. The success of the law will turn, first, on whether a political backlash dissuades plans from utilizing it and, second, whether the argument that limited cuts now are better than bigger cuts later will persuade participants not to vote down proposed reductions. Both of these considerations come together in the case of the "systemically important" Central States plan. If participants disapprove a benefit suspension, will the Treasury Department overrule them?

One recourse unhappy participants apparently do not have is litigation. MPRA denies them standing to challenge benefit suspensions in court, leaving perhaps only a potential constitutional challenge.

**The Regulations**

Desiring speedy action, Congress gave Treasury and the PBGC a 180-day deadline for issuing regulations to implement MPRA. On June 17, they released three sets of pertinent rules some three days after that deadline. The Treasury's portion consisted of temporary and proposed regulations on the standards and procedures for benefit suspensions, and the PBGC's portion consisted of an interim final rule on partitions. Simultaneously, Treasury took two additional steps: The IRS published Revenue Procedure 2015-34, which provides additional details concerning applications for benefit suspensions, including a model notice to plan participants, and Kenneth R. Feinberg, who oversaw TARP and various programs to compensate disaster victims, was appointed as "special master" for reviewing suspension applications.

Treasury's issuance of separate temporary and proposed regulations is largely a formality. The temporary regulations include the guidance needed to enable plans to submit applications for benefit suspension, but none will actually be approved until final regulations are published comprehensively addressing all of the subjects covered by the temporary and proposed regulations. In the meantime, and contrary to customary practice, plans may not rely on the proposed regulations.

Below are some of the key points of the three sets of proposed, interim, and temporary guidance, divided into benefit suspension procedure, benefit suspension substance, and plan partitions.

**ERISA Advisory – July 10, 2015**

**Procedure for Approving Benefit Suspensions**

- Applications to suspend benefits must be submitted to the Department of the Treasury, which is directed to review them in conjunction with the PBGC and the Department of Labor. Much of this task will presumably fall to the special master. Treasury has 225 days to act on applications. If it does nothing by that deadline, the application is automatically approved, subject to the outcome of the participants' vote on the suspension. The plan and Treasury may agree to extend the 225-day deadline for a decision, though the preamble discourages delay and plans would appear to have no incentive for slowing down the process.
- Notice of the application must be given to participants. The time frame for distributing this notice runs from four business days before to four business days after the application is submitted. The preamble to the temporary regulations suggests waiting until Treasury confirms that the submission is complete and promises that completeness will be determined within two business days. Notices to participants may be distributed by mail or electronically. The likelihood that electronic distribution to any large proportion of participants will be practicable is low.
- The temporary regulations detail the content of the notice. Among the mandatory items is an "individualized estimate, on an annual or monthly basis, of the effect of the suspension." Performing the necessary calculations for tens or hundreds of thousands of persons entitled to current or future benefits may be a formidable challenge.
- The notice must be provided to all participants, beneficiaries of deceased participants, and alternate payees under qualified domestic relations orders, including those whose benefits will not be affected by the suspension. The plan must make "reasonable efforts" to locate all persons who are supposed to receive the notice. "Reasonable efforts" are specified as including requesting information from the union that represents participants and from the companies that employed them, supplemented by such resources as "an Internet search tool, a credit reporting agency, and a commercial locator service." Again, the required tasks may be formidable. Few large multiemployer plans keep close track of participants.
- The proposed effective date of the benefit suspension may not be earlier than the date of partition, if the plan is also applying for that relief, or nine months after the submission of the application, if no partition is planned. The proposed date may or may not be the final one. Suspensions cannot go into effect until after participants vote to approve them (or their negative vote is overridden by Treasury).
- The electorate for the suspension vote consists of all participants and beneficiaries of deceased participants who can be located through "reasonable efforts." Alternate payees are not eligible. The suspension is approved unless rejected by a majority of the eligible voters; abstentions thus count as "yes" votes. The statute and the proposed regulations spell out in detail information that must be included on the ballot. While the plan prepares the ballot, it must be approved by the three ERISA agencies. Beyond that, the administration of the vote is left for later guidance.
- A plan with 10,000 or more participants that applies for benefit suspension must select a retired participant in pay status as a "retiree representative" whose role is "to advocate for the interests of the retired and deferred vested participants and beneficiaries of the plan throughout the suspension approval process." The temporary regulations authorize, but do not require, plans to continue the representative's functions after a suspension is approved. Smaller plans are also allowed to create the position. Exactly what the retiree representative will do remains vague, and no attempt has been made to delineate the scope of the representative's duties to his or her constituency. Making the position yet more mysterious is the fact that a plan trustee (that is, someone who very likely helped design the suspension) may be selected to fill it.

**Substantive Rules Governing Benefit Suspensions**

- The fundamental conditions that a proposed benefit suspension must satisfy are, first, that its implementation will prevent the plan from becoming insolvent and, second, that the suspension is not materially larger than what is needed to avoid insolvency. For the first condition, the proposed regulations set forth a three-part test:

  1. The plan's resources must be projected to be at least sufficient to pay benefits as they come due throughout the next 30 years, beginning with the year of the suspension. (In some cases, the 30-year period is extended.)
  2. The probability that the plan will remain solvent throughout the 30-year period, projected for a wide variety of assumed variations in investment return, must be greater than 50%. Only plans with 10,000 or more participants are subject to this condition.
  3. Either the plan must be projected to be fully funded at the end of the 30-year period, or the projection must show that, during the last five years of the period, neither available resources nor the ratio of resources to benefit payments will decline.

  The condition that the suspension be the minimum necessary to ensure continued solvency is automatically satisfied if the PBGC approves a partition of the plan (because maximum benefit suspension is a prerequisite to partition). Otherwise, up to five percent leeway is permitted between the proposed suspension and one that would result in projections that would show the conditions for suspension to be exactly met.

- The proposed regulations discuss rather vaguely the standards for determining whether the distribution of benefit suspensions among different classes of participants is "equitable," but they do offer a number of examples. The general principle underlying the examples is that unequal suspensions may be equitable if they favor older participants, participants in pay status, or participants with smaller pensions, or if they reduce or eliminate post-retirement cost-of-living increases, past benefit increases or "thirteenth checks," or if a lesser reduction for a particular class is essential to securing its votes in favor of the suspension. Example of inequitable distributions include a special dispensation for employees of a company that is represented on the board of trustees and an arbitrarily large suspension for participants who worked for employers that withdrew in the past, went into bankruptcy and failed to pay their full withdrawal liability. The equitable distribution requirement also applies to any benefit improvements for participants in pay status that may be adopted during the period of benefit suspension.

- Plans have great flexibility in fashioning suspensions, which may be permanent or temporary, may change over time, or may affect different groups of participants differently. The proposed regulations do, however, forbid changes based on contingent events. A suspension could not, for example, be increased or diminished automatically if the plan's funded status improved or deteriorated beyond specified levels.

- Every year, the plan's trustees must determine whether the benefit suspension is still necessary in order for the plan to avoid insolvency. If it is not, it must be ended. If the plan's position has improved, so that a lesser suspension would avoid insolvency, the suspension *may* be reduced for participants who are in pay status. (It should also be noted that partitioned plans must pay additional PBGC premiums if they reduce suspensions or otherwise improve benefits.) Reductions short of elimination are not mandatory.

- Annually, the trustees also must ascertain and take any other reasonable measures, aside from the benefit suspension, that will help avoid insolvency. The determinations that the continuation of the suspension is necessary and that all reasonable measures to avoid insolvency have been taken must be documented in writing. Failure to do so results in the cancellation of the suspensions, a drastic punishment that is likely to affect innocent participants more severely than the malefactors.

- Benefit improvements for participants who are not yet in pay status and that result in more than a *de minimis* increase in plan liabilities are allowed only if accompanied by an increase for pay-status participants that results in at least an equal liability increase.

- Several provisions of the proposed regulations clarify the age and disability limitations on benefit suspensions:
  - Addressing an ambiguity in the statute, the proposed regulations state that the entire pension that a participant receives upon becoming disabled is ineligible for suspension, not just the portion in excess of the pension that the participant would otherwise have received. Moreover, the disability pension retains its character after the participant reaches normal retirement age, even if the plan technically starts paying the participant a normal retirement benefit rather than a disability benefit at that point.
  - Whether a pension is for disability depends solely upon its characterization by the plan. The proposed regulations do not limit it to Social Security disability or some other uniform standard.
  - If a participant who is receiving a joint-and-survivor annuity is over age 75 when a suspension goes into effect, the suspension is limited for both the participant and, after his or her death, for their beneficiary, regardless of the beneficiary's age.
  - The age-based limitation for an alternate payee under a separate interest Qualified Domestic Relations Order (QDRO) is based on the alternate payee's age at the time of the suspension, without regard to the participant's age. Under a shared interest QDRO, the participant's age controls.
  - If the suspension is increased after it initially goes into effect, the age-based limitations are, as a general rule, recalculated on the basis of ages at the new effective date.

**Partitions and PBGC Financial Assistance**

- The PBGC's regulation on partitions has one large, though perhaps unavoidable, lacuna. As stated in the preamble:

  > A number of commenters requested guidance on PBGC's evaluation criteria and standards for approval. PBGC considered these comments, but concluded that given the nature of the analysis and determinations required under section 4233(b) of ERISA with respect to both the plan applicant and PBGC, it is not able to provide guidance in those areas at this time. As a result, PBGC will review each application for partition on a case-by-case basis in accordance with the statutory criteria in section 4233(b). Such experience may enable PBGC to develop appropriate guidance in those areas in the future.

  The essence of the statutory criteria is that the partition must be necessary for the plan to remain solvent, must reduce the PBGC's anticipated long-term losses and must not impair the PBGC multiemployer insurance fund's ability to meet its other obligations. The crucial question will be how the PBGC evaluates the long-term impact of immediate expenditures to shore up a partitioned plan. The only way to reduce the PBGC's eventual losses is for the plan to gain the capacity to pay more benefits than anticipated at the time of the partition. It may be hard to demonstrate that the PBGC, by taking on some liabilities at an early stage, will ultimately increase the plan's assets.

- What the interim final regulation *does* cover is "the process for submitting an application for partition, the information required to be included in an application, notice requirements under section 4233(a)(2), including the form and manner of the notice, the notification process for PBGC decisions on applications for partition, the content of a partition order, and the scope of PBGC's continuing jurisdiction under a partition order." Most of these provisions are straightforward. The information demanded from the plan contains no surprises, and the PBGC has given itself a 270-day deadline for approval or rejection. One noteworthy point is that decisions are not subject to the internal PBGC appeals process.

- Because a partition is possible only in conjunction with a benefit suspension, the regulation coordinates the applications to the PBGC for the former and to Treasury for the latter. *Inter alia* notices informing participants of both applications may be issued together, and a partition may be approved contingent upon final approval of the accompanying benefit suspension. Coordination is optional and is even described as a "special rule," but it is hard to imagine that many plans will fail to take advantage of it.

- A partition results in two plans, the original plan and a new one, to which the regulation gives the name "successor plan." The successor plan will exist as a ward of the PBGC, with no assets, no contributing employers and no share of withdrawal liability payments owed to the original plan. Its sole source of funds will be "loans" from the PBGC to pay benefits as they become due. The regulation leaves the original plan free to allocate benefits to the successor plan in any manner, so long as transfer is limited to the minimum value of benefits needed to keep the original plan from insolvency. Participants will have no reason to care which plan is responsible for their benefits. Any amount to which they are entitled above the PBGC guarantee level (which is all that can be paid by the successor plan) will continue to be paid by the original plan. The regulation permits the two plans to combine benefit payments so that each participant receives only one check each month.

- For the first 10 years after a partition, withdrawal liability for employers that leave the original plan must be calculated by taking into account the unfunded vested benefits of both the original and the successor plan. After 10 years, withdrawal liability calculations will disregard the successor plan. Neither the statute nor the regulation explains what that means. If the plan uses the presumptive method of allocating UVB's, are liability change pools for past years adjusted after the 10-year mark as if the successor plan benefits had never been part of the original plan? Happily, plenty of time remains to consider the answer before the question can arise.

- The regulation grants the PBGC continued jurisdiction over partitions after they are implemented, including the right to amend partition orders after the fact.

- It remains to be seen how useful the PBGC's expanded partition authority will be to troubled plans or to the PBGC. The prior type of partition, which separated a bankrupt employer's participants from the rest of the plan, had potential but was hardly ever utilized in practice. The new type is essentially accelerated financial assistance, as the partition is little more than a legal fiction. The attraction for plans is obvious, but the question to consider remains: will the PBGC be able to save money in the long run by paying more in the short run?