Impact of the Pension Protection Act of 2006 on Multiemployer Plan Funding

May 3, 2007
Technical Changes and General Observations

General Changes

- **Funding Standard Account remains intact**
  - Amortization bases for changes in plan benefits reduced from 30 to 15 years (or shorter, depending on payout period)
  - Amortization for changes in assumptions or methods reduced from 30 to 15 years
  - Automatic extension (for up to five years) of amortization period for charge bases (additional five years available upon application provided certain conditions are met)

- **Actuarial assumptions**
  - Must be reasonable both in the aggregate and individually

- **Annual actuarial certification required to determine “Zone” status**
  - Critical (aka Red Zone)
  - Endangered/Seriously Endangered (aka Yellow Zone)
  - Neither of these (aka Green Zone) – no certification required

- **Higher tax-deductible limit**

- **Increased disclosure**
  - Expanded detail in annual funding notice to participants and employers
  - Explanatory notices, data and updates for plans in endangered or critical status
  - More information to employers and participants, on request
  - Employee benefit statements more accessible
  - More detail on withdrawal liability estimates
  - Expanded 5500 information
Observations

- **Long-term perspective required**
  - Structure imposed to identify and address funding problems early
  - Move away from sole focus on immediate funding deficiency
  - Financial improvement plans span 10+ years

- **Trustees’ role expanded and changed**
  - Rules of stewardship apply
  - Responsibility to develop and adopt formal financial improvement plans
  - More accountability
  - More authority

- **Additional flexibility and discipline**
  - In some situations “adjustable benefits” may be reduced
  - Restructure benefits to obtain long-term balance with contributions
  - Reject agreements not consistent with plan’s financial health
  - Shortened amortization periods
  - Excise taxes for non compliance
Red Zone Plans

Zone determination

- Critical Status
  - Tests
    » Funding deficiency in four or five years OR
    » A cash-flow crisis in five to seven years
  - Notice to participants, unions, employers and government
  - Trustees must develop, adopt and present a “Rehabilitation Plan” to the bargaining parties

“Rehabilitation Plan”

- Up to $1,100 / day penalty on Board of Trustees for failure to timely adopt
- Collective bargaining process remains intact
- Benefit and contribution schedules provided to bargaining parties
- Trustees can not accept collective bargaining agreements inconsistent with Rehabilitation Plan objectives and benchmarks
Red Zone Plans – continued

New Tools

• Reduction/elimination of “adjustable benefits” (e.g., early retirement subsidies and certain other protected benefits)

• Temporary contribution surcharges on employers

• Shelter from excise tax on funding deficiencies if in compliance with Rehabilitation Plan

• 5-Year amortization extension on charge bases
Yellow Zone Plans

- **Zone determination**
  - **Endangered Status**
  - **Tests**
    - Less than 80% funded and/or funding deficiency within seven years
    - If both, then seriously endangered
    - Notices as in Red Zone
    - Trustees must develop, adopt and present a “Funding Improvement Plan” to the bargaining parties

- **“Funding Improvement Plan”**
  - Benefits and contribution schedules provided to bargaining parties
  - Reduce underfunding by 1/3 over 10 years (or 1/5 over 15 years)
  - Can not have a funding deficiency
  - Penalty for failure to timely adopt
  - Trustees can not accept collective bargaining agreements inconsistent with Funding Improvement Plan objectives and benchmarks

- **Fewer “New Tools”**
  - 5-Year amortization extension on charge bases
PPA and Timeline for a Calendar Year Plan

- **Actuary Certifies Zone Status 3/30/2008**
  - **Yellow or Red**
  - **Notice to Stakeholders of Critical or Endangered Status 4/29/2008**
  - **Red**
  - **Trustees Adopt Funding Improvement Plan 11/25/2008**
  - **Yellow**
  - **Provide Schedules to Bargaining Parties Effective When Negotiated 12/25/2008**
  - **Red**
  - **Provide Summary of Financial Improvement Plans to Stakeholder 4/30/2009**
- **Temporary 5% Surcharge on Employers 5/29/2008**
- **Trustees Adopt Rehabilitation Plan 11/25/2008**
- **5% Surcharge Increases to 10% 1/1/2009**
- **Monitor and Change as Needed**

- **Home Free (at least for one year)**
Various Perspectives on PPA

➢ Trustees
  - Forces to look at long-term funding issues they have been slow to address in some cases
  - More responsibility/risk
  - Greater need to become educated in actuarial details
  - Concerned about equity with respect to collective bargaining agreement effective dates for plan changes
  - Potential for multiple benefit schedules

➢ Employer perspective
  - Greater risk for additional contributions
  - More tools to look at funding over the long term
  - Ability to stay competitive with non-union businesses
  - Heightened sensitivity to total payroll costs and impact of benefit design
  - Very concerned about surcharges

➢ Unions and Participants
  - Greater risk of lower benefits, especially in Red Zone
  - New hires to subsidize current participants
  - “Continuous” cycle of benefit reductions
  - Create dissatisfaction with compensation package