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Proposed Multiemployer Composite Plans: Background and Analysis

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March 27, 2017

Congressional Research Service
7-5700
www.crs.gov
R44722

CRS REPORT
Prepared for Members and
Committees of Congress

Summary

Multiemployer pension plans are sponsored by more than one employer in the same industry and are maintained as part of a collective bargaining agreement. The challenges facing one type of multiemployer plans—defined benefit (DB) plans, in which participants receive regular monthly benefit payments in retirement—have led stakeholders to seek alternative pension plan designs that could alleviate some of the concerns but retain some of the beneficial features.

On September 9, 2016, Representative John Kline, chairman of the House Committee on Education and the Workforce in the 114th Congress, issued a discussion draft of a bill that would authorize a new multiemployer pension plan called a *composite plan*. A composite plan would be neither a DB pension nor a defined contribution (DC) pension (such as 401(k) plans, in which participants have individual accounts that are the basis of income in retirement). Since composite plans would be neither DB nor DC plans, authorizing legislation would be necessary to implement the proposal.

The composite plan proposal is the third element of a proposal by representatives of an organization of multiemployer pension and health plans to reform multiemployer DB pension plans. The first two elements were adopted as the Multiemployer Pension Reform Act of 2014 (MPRA, enacted as Division O in the Consolidated and Further Continuing Appropriations Act, 2015; P.L. 113-235). These elements consist of (1) proposals to strengthen the current multiemployer system and (2) measures to assist plans in very poor financial condition.

The main features of a composite plan include the following:

- Employer contributions would generally be a stable amount and would not need to increase in response to investment losses.
- Participants would receive monthly benefits for the lifetime of the participant (and spouse, if married).
- Participants' benefits could decrease if the plan's assets experienced investment losses.
- Composite plans would not be covered by Pension Benefit Guaranty Corporation (PBGC) insurance and would not receive financial assistance from PBGC if a composite plan were to become insolvent and unable to pay participants' benefits.
- Composite plans would not feature withdrawal liability, which is an exit fee employers in underfunded multiemployer DB plans must pay to leave the plan.

For employers, composite plans would offer several advantages over DB plans. For example, employers would not have to pay withdrawal liability when leaving the plan and the plan would not have to pay PBGC insurance premiums. In addition, the likelihood of stable contributions likely would be an attractive feature.

Retired participants in composite plans would receive monthly benefit payments. However, the benefit amounts could increase or decrease, depending on the investment experience of the plan. The composite plan proposal contains a procedure to address situations in which plan assets fall below 120% of plan liabilities, such as could occur if there were investment losses. This *realignment program* includes proposed, though not mandatory, contribution increases and mandatory benefit reductions.

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On September 9, 2016, Representative John Kline, chairman of the House Committee on Education and the Workforce in the 114th Congress, issued a discussion draft of a bill that would authorize a new multiemployer pension plan called a *composite plan*.[1] A composite plan would contain features of two types of existing pension plans: (1) defined benefit (DB), in which participants receive regular monthly benefit payments in retirement (which some refer to as a "traditional" pension), and (2) defined contribution (DC) plans (of which the 401(k) plan is the most common), in which participants have individual accounts that are the basis of income in retirement.[2] Since composite plans would be neither DB nor DC plans, authorizing legislation is necessary to implement the proposal.

This report provides background on multiemployer pension plans; summarizes the discussion draft authorizing composite plans and explains the main features of these proposed plans; and explores various policy discussions surrounding composite plans, including their potential benefits and drawbacks for employers and employees, their possible implications for the Pension Benefit Guaranty Corporation (PBGC), and their potential effects on the broader retirement system.

Background on Multiemployer Pensions

In addition to being classified as DB or DC plans, pension plans are also classified by whether they are sponsored by one employer (single-employer plans) or by more than one employer (multiemployer and multiple employer plans). Multiemployer pension plans are sponsored by employers in the same industry and maintained as part of a collective bargaining agreement.[3]

In 2013, there were 1,435 multiemployer DB pension plans that covered 10.4 million participants.[4] These plans had $422.9 billion in assets and owed participants $1.0 trillion in benefits for a total amount of underfunding of $610.8 billion.[5]

Multiemployer plans that meet specified financial criteria are required to report to the Internal Revenue Service (IRS) their financial condition as being in one of several categories. The categories are (1) *endangered* (or a subcategory called *seriously endangered*) (both are sometimes called "yellow zone"),[6] (2) *critical* (sometimes called "red zone"),[7] and (3) critical and declining.[8]

[1] The draft is available at http://edworkforce.house.gov/uploadedfiles/composite_a_xml.pdf. Virginia Foxx, chair of the House Committee on Education and the Workforce in the 115th Congress, has reportedly endorsed the composite plan proposal. See Kimberly Hefling, Marianne Levine, and Michael Stratford, "Virginia Foxx makes play for House Education and Labor committee chairmanship," *Politico*, September 13, 2016, at http://www.politico.com/story/2016/09/virginia-foxx-makes-play-for-house-education-and-labor-committee-chairmanship-228073.

[2] In some DB plans, plan participants have the option to receive a lump-sum payment at retirement in lieu of the annuity. An annuity is a monthly payment for life. In some DC plans, plan participants have the option to purchase annuities with some or all of their account balances.

[3] Multiple employer plans are sponsored by more than one employer but are not maintained as part of a collective bargaining agreement. Multiple employer pension plans are not common and not covered by any of the provisions in the discussion draft. The Government Accountability Office (GAO) indicated that about 0.7% of private-sector pension plans were multiple employer pension plans. See U.S. Government Accountability Office, Federal Agencies Should Collect Data and Coordinate Oversight of Multiple Employer Plans, GAO-12-665, September 13, 2012, p. 10, at http://www.gao.gov/assets/650/648285.pdf.

[4] See Pension Benefit Guaranty Corporation, *2014 Pension Insurance Data Tables*,Table M-6, http://www.pbgc.gov/documents/2014-data-tables-final.pdf.

[5] Among underfunded plans, the amount of underfunding was $611.1 billion. Among overfunded plans, the amount of overfunding was $299 million. See Pension Benefit Guaranty Corporation, 2014 Pension Insurance Data Tables,Table M-9, http://www.pbgc.gov/documents/2014-data-tables-final.pdf.

[6] A plan is in endangered status if (1) the plan's funding ratio is less than 80% funded or (2) the plan has a funding (continued...)

Plans that do not meet the criteria for any of these categories are sometimes referred to as being in the "green zone". In 2014, PBGC reported that 164 plans were in endangered or seriously endangered status, 323 plans were in critical status,[9] and 779 in green zone status.[10]

Congress approved changes to multiemployer DB pension funding rules in the Multiemployer Pension Reform Act of 2014 (MPRA, enacted as Division O in the Consolidated and Further Continuing Appropriations Act, 2015; P.L. 113-235).[11] Among other provisions, plans in critical and declining status may be eligible to apply to the Department of the Treasury to reduce benefits. MPRA did not address new pension plan structures, such as composite plans.[12] Some Members of Congress have indicated that the proposal for composite plans is a continuation of the work done in MPRA.[13]

Pension Benefit Guaranty Corporation Insurance

The Pension Benefit Guaranty Corporation (PBGC) was established by the Employee Retirement Income Security Act of 1974 (ERISA; P.L. 93-406) to insure benefits in private-sector DB

(...continued)

deficiency in the current year or is projected to have one in the next six years. A plan is seriously endangered if it meets both of these criteria. The funding ratio is the amount of plan assets divided by the value of plan liabilities. A pension plan's assets are primarily investments purchased with employer contributions and accumulated investment earnings. A plan's liabilities are primarily future benefit obligations calculated as a present value.

7 A plan is in critical status if any of the following conditions apply: (1) the plan's funding ratio is less than 65% and in the next six years the value of the plan's assets and contributions will be less than the value of benefits; (2) in the current year, the plan is not expected to receive 100% of the contributions required by the plan sponsor, or the plan is not expected to receive 100% of the required contributions for any of the next three years (four years if the plan's funding percentage is 65% or less); (3) the plan is expected to be insolvent within five years (within seven years if the plan's funding percentage is 65% or less); or (4) the cost of the current year's benefits and the interest on unfunded liabilities are greater than the contributions for the current year, the present value of benefits for inactive participants is greater than the present value of benefits for active participants, and there is expected to be a funding deficiency within five years.

8 Among plans that are in critical status, a plan is in declining status if the plan actuary projects the plan will become insolvent within the current year or, depending on certain circumstances as specified in 26 U.S.C. 432, within either the next 14 years or 19 years.

9 Critical and declining status was not reported by plans until 2015.

10 See Pension Benefit Guaranty Corporation, "Multiemployer Supplement 2015 Data Tables," https://www.pbgc.gov/documents/2015-PBGC-Data-Tables-Multiemployer-Supplement.pdf. PBGC does not indicate why number of certifications received is less than total number of multiemployer DB pension plans. PBGC had previously indicated that the total number of plan certifications is less than the total number of multiemployer defined benefit pension plans because some plans are terminated but continue to pay benefits (wasting trusts) and are required to file annual Form 5500 reports but are not required to file zone certifications. See Pension Benefit Guaranty Corporation (PBGC), Multiemployer Pension Plans: Report to Congress Required by the Pension Protection Act of 2006, January 22, 2013, p. 40, at http://www.pbgc.gov/documents/pbgc-report-multiemployer-pension-plans.pdf.

11 For more information on MPRA, see CRS Report R43305, *Multiemployer Defined Benefit (DB) Pension Plans: A Primer and Analysis of Policy Options*, by John J. Topoleski.

12 See House Committee on Education and the Workforce, "Kline Releases Discussion Draft to Modernize Multiemployer Pensions," press release, September 9, 2016, at http://edworkforce.house.gov/news/documentsingle.aspx?DocumentID=400989.

13 See, for example, Opening Statements by Representative Phil Roe and Representative Jared Polis, U.S. Congress, House Committee on Education and the Workforce, Subcommittee on Health, Employment, Labor, and Pensions, *Examining Reforms to Modernize the Multiemployer Pension System*, 114th Cong., 1st sess., April 29, 2015, at http://edworkforce.house.gov/calendar/eventsingle.aspx?EventID=398718.

pension plans.[14] It operates two insurance programs: one for single-employer pension plans and a second for multiemployer pension plans. The two programs operate independently of each other.

When a multiemployer DB pension plan becomes insolvent, PBGC provides financial assistance to the plan to pay participants' benefits. When a multiemployer plan receives financial assistance from PBGC, the plan must reduce participants' benefits to a maximum per participant benefit as set in statute.[15] The maximum benefit is calculated as: 100% of the first $11 of the monthly benefit rate, plus 75% of the next $33 of the monthly benefit rate, times the participant's years of credited service. For example, an individual with 30 years of service in the plan could receive a maximum benefit of [30 × (100% × $11 + 75% × $33)] = $12,870 per.[16] The benefit is lower for individuals with less than 30 years of service in the plan.

PBGC's multiemployer program receives funds from premiums paid by participating employers ($282 million in FY2016) and from the income from the investment of unused premium income ($143 million in FY2016). The poor financial condition of some multiemployer DB pension plans threatens the solvency of PBGC's multiemployer insurance program. There are no provisions in law that provide for assistance from the U.S. Treasury in the event of PBGC's insolvency. ERISA states that "the United States is not liable for any obligation or liability incurred by the corporation."[17]

At the end of FY2016, PBGC reported a deficit of $58.8 billion in the multiemployer insurance program.[18] If a sufficient number of multiemployer pension plans exhaust their plan assets and become unable to pay promised benefits, it is likely that PBGC would also exhaust its assets. PBGC indicated that there is more than a 50% chance of PBGC insolvency by the end of 2025, a more than 90% chance of insolvency by the end of 2028, and a 98% chance of insolvency by 2035.[19]

The Congressional Budget Office (CBO) provided several estimates of PBGC's financial condition.[20] CBO's *cash-based* estimates account for spending and revenue in the years when they are expected to occur. CBO estimates that from 2017 to 2026, PBGC will be obligated to pay $9 billion in claims but will only have sufficient resources to pay $6 billion. From 2027 to 2036, claims to PBGC will be $35 billion but PBGC will only have sufficient resources to pay $5 billion. CBO also provided *fair-value* estimates, which are the present value of all expected future claims for financial assistance, net of premiums received.[21] CBO's fair-value estimate of PBGC's future obligations was $101 billion.

[14] ERISA was enacted in 1974 to provide a comprehensive federal scheme for the regulation of employee pension and welfare benefit plans offered by private-sector employers. More information is available is CRS Report RL34443, *Summary of the Employee Retirement Income Security Act (ERISA)*, by Patrick Purcell and Jennifer A. Staman.

[15] See ERISA 4022A(c).

[16] The PBGC maximum benefit for participants in multiemployer pension plans is not adjusted annually for inflation.

[17] See 29 U.S.C. 1302(g)(2).

[18] See PBGC FY2016 Annual Report available at http://www.pbgc.gov/Documents/2016-annual-report.pdf.

[19] See PBGC MPRA Report, at http://pbgc.gov/documents/MPRA-Report.pdf.

[20] Congressional Budget Office, *Options to Improve the Financial Condition of the Pension Benefit Guaranty Corporation's Multiemployer Program*, 51356, August 2016, https://www.cbo.gov/publication/51536.

[21] Present value is the current value of a future sum of money. For an explanation of present value in the context of a pension plan, see the appendix to CRS Report R43305, *Multiemployer Defined Benefit (DB) Pension Plans: A Primer and Analysis of Policy Options*.

Overview of the Discussion Draft

As a result of the challenges facing multiemployer DB pension plans, stakeholders have sought alternative pension plan designs that could alleviate some of the concerns but retain some of the beneficial features. These alternative plan designs would need to be authorized in ERISA.[22]

The Canadian government and several provinces in Canada have been considering or implementing the regulatory changes needed for employers to more widely adopt alternative plan structures, which are referred to as target benefit plans in Canada.[23] The proposal for composite plans for plan sponsors in the United States was included in *Solutions Not Bailouts*, a 2013 report by a coalition of labor and management groups organized by the National Coordinating Committee for Multiemployer Plans (NCCMP), an organization of multiemployer pension and health plans.[24]

Main Features of the Proposed Composite Plan

A composite plan, as would be authorized in the discussion draft, would be neither a DB nor a DC pension plan, though it would contain elements of both. As discussed in greater detail in the following sections, the main features of the proposed composite plan would be the following:

- A participant's benefit amount would be based on a formula and payable as a life annuity.[25]
- Employer contributions[26] would remain at a fixed amount (as negotiated between labor and management) and would not be required to increase in response to underfunding.[27]
- Composite plans would be required to maintain a projected funding ratio of 120%.[28] If the amount of the plan's assets were insufficient to pay 120% of the

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[22] Two Congressional committees have held three hearings in the 114th Congress on the topic of multiemployer pension plans. See U.S. Congress, Senate Committee on Finance, *The Multiemployer Pension Plan System: Recent Reforms and Current Challenges*, 114th Cong., 2nd sess., March 1, 2016; U.S. Congress, House Committee on Education and the Workforce, Subcommittee on Health, Employment, Labor, and Pensions, *Examining Reforms to Modernize the Multiemployer Pension System*, 114th Cong., 1st sess., April 29, 2015; and U.S. Congress, House Committee on Education and the Workforce, Subcommittee on Health, Employment, Labor, and Pensions, *Discussion Draft to Modernize Multiemployer Pensions*, 114th Cong., 2nd sess., September 22, 2016.

[23] See, for example, Government of Canada, Department of Finance, *Consultation Paper - Pension Innovation for Canadians: The Target Benefit Plan*, at https://www.fin.gc.ca/activty/consult/pic-impicc-eng.asp.

[24] More information about NCCMP is available at http://www.nccmp.org. The report is available at http://www.solutionsnotbailouts.com/.

[25] For example, a plan might pay a monthly benefit of $30 times the number of years of service in the plan. This is current practice in multiemployer DB pension plans.

[26] Nearly all contributions in private-sector DB pension plans are employer contributions. DOL data in 2011 indicated that among private-sector workers who participated in DB plans, 4% were required to make an employee contribution to the plans. See DOL, *National Compensation Survey: Employee Benefits in the United States*, March 2011, at http://www.bls.gov/ncs/ebs/benefits/2011/ebbl0048.pdf.

[27] For example, a DB pension plan can become underfunded as a result of investment losses. Under current law, employers must make up for plan underfunding.

[28] The funding ratio is the amount of plan assets divided by the value of plan liabilities. A pension plan's assets are primarily the market value of investments purchased with employer contributions and accumulated investment earnings. A plan's liabilities are primarily estimates of future benefit obligations calculated as a present value using the expected rate of return on investments as the discount rate.

promised benefits, the plan would be required to take corrective action to restore the funding ratio to 120%.

- The options for corrective actions (called a *realignment program* in the discussion draft) include possible employer contribution increases (if agreed to by the bargaining parties) and reductions to participants' benefits.[29]

- Composite plans would *not* be covered by PBGC. Therefore, plan sponsors would not pay PBGC premiums and participants' benefits would not be protected if the plan were to become insolvent.
- Composite plans would *not* feature withdrawal liability. Withdrawal liability is a payment or series of payments by an employer that seeks to no longer participate in a multiemployer DB pension plan. The calculation of withdrawal liability is based on the employer's share of unfunded benefits that are owed to participants in the plan.

An existing multiemployer DB pension plan could adopt a composite plan while maintaining an existing DB plan. The existing plan is referred to as a *legacy plan* in the discussion draft. The main features of a legacy plan would be

- participants in a legacy plan whose employers opted for the composite plan would cease to earn benefits in the legacy plan and begin to earn benefits in the composite plan;[30] and
- employers would generally be required to contribute to the legacy plan at minimum funding levels (called a *transition contribution rate* in the discussion draft). The minimum funding levels should, in principle, restore the legacy plan to a 100% funding level over time.

Key Provisions in the Discussion Draft

This section summarizes in greater detail the main provisions in the discussion draft.[31] The draft authorizes the creation of multiemployer composite plans and establishes the requirements that composite plans would have to meet. The draft also establishes rules for existing multiemployer DB plans to which composite plans would be added.

[29] Apart from the benefit reductions allowed under MPRA, ERISA Section 204(g) generally prohibits a pension plan from reducing or eliminating participants' earned benefits (called the *anti-cutback rule*). For more information, see CRS Report RL34443, *Summary of the Employee Retirement Income Security Act (ERISA)*, by Patrick Purcell and Jennifer A. Staman.

[30] The discussion draft does not contain any provisions to transfer benefit obligations from legacy plans to composite plans. Some discussions in Canada have considered whether to allow the conversion of the DB pension to a target benefit plan, which could subject these benefits to being reduced in the event of funding shortfalls. For more information, see Department of Finance - Canada, *Consultation Paper Pension Innovation for Canadians: The Target Benefit Plan Section 4.8. Conversion of Pension Plans to Target Benefit Plans,* April 2014, at https://www.fin.gc.ca/activty/consult/pic-impicc-eng.asp#toc372117662.

[31] Additional summaries are available at House Committee on Education and the Workforce, *Section-By-Section Summary of the Draft Proposal to Modernize Multiemployer Pensions*, at http://edworkforce.house.gov/uploadedfiles/section-by-section.pdf; House Committee on Education and the Workforce, *Summary of a Discussion Draft to Moderninze Multiemployer Pensions*, at http://edworkforce.house.gov/uploadedfiles/discussion_draft_summary_-_multiemployer_composite_plans.pdf; House Committee on Education and the Workforce, *Basic Q&As on a Discussion Draft to Modernize Multiemployer Pensions*, at http://edworkforce.house.gov/uploadedfiles/basic_q_and_as_on_a_discussion_draft.pdf; and Segal Consulting, *Multiemployer "Composite Plan" Draft Legislative Language Released*, August 15, 2016, at https://www.segalco.com/media/2694/me-9-15-2016.pdf.

Legislation that affects private-sector pensions often amends both Title 29 (Labor Code) and Title 26 (Internal Revenue Code [IRC]) of the *U.S. Code*. The provisions in the discussion draft that amend the IRC are identical or nearly identical to the provisions that amend the Labor Code. Therefore, the IRC provisions are not included in this more detailed summary. For ease of comparison, the headings in this summary generally align with the headings in the discussion draft.

Requirements for a Composite Plan

A composite plan would be an employer-sponsored multiemployer pension plan that would be neither a DB plan (in which the benefit is fixed and cannot be reduced except under MPRA) nor a DC plan (in which participants have ownership of funds in an account).

A composite plan would systematically pay benefits that would be calculated according to a formula specified in the plan.[32] The benefit would be a monthly payment beginning at retirement and lasting for the life of the participant (and spouse, if married).

In the first year of the composite plan, the employer's contribution would be 120% of the plan's normal cost.[33]

Each year, the plan would make two actuarial determinations of the plan's financial condition: (1) current funded ratio (CFR) and (2) projected funded ratio (PFR). These will be defined in the next section, *Funded Ratios; Actuarial Assumptions,* of this report.

If the plan's PFR were less than 120%, the plan would be required to take corrective action.

The plan's trustees would include a retiree or beneficiary who would be receiving benefits from the plan.[34]

A composite plan could be added as a component to an existing multiemployer plan or could be adopted as a stand-alone plan, provided the multiemployer DB plan is not in critical status nor is expected to be for the next five years.

If a composite plan were to be added to a multiemployer plan, the composite plan and multiemployer plan would be maintained as separate plans. The assets of each plan could be held in a single trust provided separate accounts were maintained. The plans could, but would not be required to, pool their assets.

The assets of each of the plans would be held, invested, reinvested, managed, administered, and distributed for the exclusive benefit of the participants and beneficiaries of each component. The assets of one component could not be used to pay for the benefits of the other component.

Funded Ratios; Actuarial Assumptions

Each year, a composite plan would report its CFR and PFR.

CFR would be calculated as the market value of plan assets divided by the present value of plan liabilities.

[32] The formula typically multiplies a dollar amount by the number of years of service the employee has worked for employers that participate in the DB plan.

[33] A pension plan's normal cost is the amount of new benefits earned by participants.

[34] If less than 5% of the participants in the plan are receiving benefits, this requirement does not apply.

PFR would be the CFR projected 15 years into the future. The PFR could incorporate anticipated contribution increases of up to 2.5% per year.

Costs, liabilities, and rates of interest would (1) use reasonable assumptions (taking into account the plan's experience and reasonable expectations) and (2) offer the best estimate of the plans anticipated experience.[35]

Any changes to actuarial assumptions from the previous year would be documented by the plan actuary.

The value of plan assets would be at market values.[36]

The value of plan liabilities would use the unit credit funding method. The unit credit funding method is commonly used by multiemployer DB pension plans.[37]

Realignment Program

If a composite plan's PFR were less than 120%, then the plan would have to adopt a realignment program. A realignment program would be a range of options that the plan sponsor or bargaining parties could undertake to achieve a PFR of 120% the following year.[38]

The initial elements of a realignment program could, but are not required to, include

- proposed employer contribution increases;
- reductions in the rate of future benefit accruals;
- modification or elimination of adjustable benefits for participants not currently receiving benefits from the plan; and
- other lawfully available measures.[39]

If these measures would not enable the plan to achieve 120% PFR, then the plan could reduce

- accrued benefits for participants who are not yet receiving benefits from the plan; and

[35] Determining whether an assumption is "reasonable" is not addressed in the discussion draft, though the term does appear elsewhere in ERISA. See, for example, ERISA §304 and Pension Committee of the Actuarial Standards Board, *Selection of Economic Assumptions for Measuring Pension Obligations*, September 2013, at http://www.actuarialstandardsboard.org/wp-content/uploads/2014/02/asop027_172.pdf.

[36] The market value is the dollar amount at which a financial security or other asset can be easily sold. For more information on asset valuation in pension plans see Society of Actuaries, *Pension Plan Asset Valuation Methods*, August 2001, at https://www.soa.org/Library/Newsletters/Pension-Forum/2001/August/pfn-2000-vol13-iss1-haberman-owadally.aspx.

[37] For more information on the unit cost method, see American Academy of Actuaries, *Fundamentals of Current Pension Funding and Accounting For Private Sector Pension Plans*, July 2004, at https://www.actuary.org/pdf/pension/fundamentals_0704.pdf.

[38] Because benefits in composite plans are not guaranteed, some might suggest that a composite plan's investment strategy (e.g., the amounts and types of plan investments) should be more conservative than in a traditional DB pension plan. For example, composite plans could invest less in equities (like company stock) and more in debt instruments (such as U.S. Treasury and corporate bonds). However, the tradeoff for a more conservative investment policy would be lower promised benefits. More conservative investments such as bonds generally have lower investment returns than riskier investments such as company stock. However, riskier investments are also more likely have negative investment returns than conservative investments. For a discussion in the context of Canadian target benefit plans, see Aon Hewitt, *Investments for the Target Benefit Plan*, 2015, at https://retirementandinvestmentblog.aon.com/getattachment/242ef259-eac2-4d4d-8f6d-77e2b652b555/TargetBenefitPlan-Guide4-Jan2015-EN.pdf.aspx.

[39] The discussion draft does not indicate what these measures would be.

- non-core benefits to participants who are receiving benefits from the plan.[40]

If the above measures were to fail to enable the plan to achieve 120% PFR, then the plan could

- further reduce future benefit accruals; and
- reduce core benefits to participants who are receiving benefits from the plan, provided the reductions are implemented equitably with respect to the factors listed in MPRA that allowed benefit reductions.[41]

The realignment program could specify that the benefit reduction would take effect only if the bargaining parties failed to agree to contribution increases. There is no requirement that the realignment program include contribution increases.

There would be no limitation on benefit reductions.[42]

Limitation on Increasing Benefits

The discussion draft contains provisions that would generally prohibit a composite plan from increasing benefits unless the plan was well funded.

A composite plan would not be able to increase benefits unless

- the plan's CFR was at least 110% before taking the benefit increases into account;
- the plan's CFR was at least 100% after taking the benefit increases into account;
- the plan's PFR was at least 120% after taking the benefit increases into account; and
- expected contributions for the current plan year (and assuming the benefit increases were in effect for the entire year) are at least 120% of normal cost for the year. If the plan's CFR and PFR were less than 140% after taking the benefit increases into account, the present value of plan liabilities could not increase by more than 3%.[43]

If a plan had reduced core benefits as part of a realignment program, it could (1) only increase future benefit payments[44] and (2) provide for equitable distribution of benefit increases, taking into account the benefits that had been previously reduced.

[40] Non-core benefits could include early retirement benefits, post-retirement Cost of Living Adjustments (COLAs), and benefits adopted by the plan less than 60 months before the realignment program were to take effect.

[41] Core benefits are benefits received at normal retirement age (typically aged 65) and payable as a life annuity. The factors listed in MPRA include the age and life expectancy of participants; the length of time an individual has been receiving benefits from the plan; and the years to retirement for participants who are currently working.

[42] In contrast, the following limitations apply to benefit reductions in multiemployer DB plans that receive approval from the U.S. Treasury to reduce benefits under MPRA: (1) individuals cannot have their benefits cut below 110% of the PBGC maximum guarantee, and (2) disabled individuals and retirees aged 80 or older may not have their benefits reduced. Individuals between the ages of 75 and 80 may not receive the maximum benefit reduction.

[43] These provisions would not apply if not allowing the benefit increases (1) were to jeopardize the tax qualification of the plan or (2) were to cause employer contributions to the plan to cease to be tax-deductible for employers in the plan.

[44] This would appear to preclude making up previously reduced benefits.

Composite Plan Restrictions to Preserve Legacy Plan Funding

The discussion draft allows existing multiemployer DB plans to adopt composite plans provided the plan is not in critical status or expects to be in critical status in the next five years. The existing DB plan would become a *legacy* plan, which would still be required to pay participants' benefits that had been earned in the plan.

A legacy plan would be a multiemployer DB plan that had participants who (1) ceased to earn benefits in the DB plan and (2) were eligible to earn benefits in a composite plan.

If an employer were to cease to have an obligation to a multiemployer DB plan (via a withdrawal from the DB plan), then that firm's employees would not be able to earn benefits in the related composite plan for five years after the withdrawal.

Composite plans would have to satisfy "transition contribution requirements" to ensure contributions would continue to the legacy plan.

The *transition contribution rate* would be the rate that would (1) fund the DB plan's normal cost for the plan year, (2) amortize the plan's initial unfunded liabilities over 25 years,[45] and (3) amortize subsequent unfunded liabilities over 15 years. The transition contribution rate in any given year could not be lower than the transition contribution rate in the first year.

If the status of the legacy plan were to become endangered or critical, then the transition contribution rate would be the greater of (1) the legacy contribution rate or (2) the rate determined under the funding improvement or rehabilitation plan (but not greater than 75% of the combined contribution rates to the legacy and composite plans).

The above restrictions on composite plans would cease to apply if the legacy plan (1) were fully funded in the current year, (2) had been fully funded in at least three of the previous five years, and (3) were projected to be fully funded in the following four years. The determination of fully funded would be in accordance with the determination of plan liabilities calculated as if all the employers had decided to leave the plan (referred to as a *mass withdrawal*).[46]

Mergers and Asset Transfers of Composite Plans

Composite plans would be able to merge. The resulting plan would also have to be a composite plan. A participant's accrued benefit could not be lowered as a result of the merger. Employers would continue to make contributions to legacy plans if composite plans merge.

PBGC Coverage and Withdrawal Liability

Composite plans would not be covered by PBGC insurance, nor would plan sponsors pay PBGC premiums on the composite plan portion of their multiemployer plans.

Employers in composite plans would not be subject to any withdrawal liability.

In certain circumstances, employers in legacy plans would not have any withdrawal liability. A legacy plan would have no withdrawal liability if the plan (1) were fully funded for three of the

[45] Amortization means that plans can spread out the effect of these events over a specified number of years. Currently, unfunded liabilities in multiemployer DB plans may be amortized over 15 years. This provision allows employers to contribute less to their plans in a given year than they otherwise would. Allowing a longer amortization period is sometimes called a *fresh start*.

[46] Withdrawal liability on a mass withdrawal basis is typically larger than on an ordinary basis. Among the reasons is that the discount rates used to calculate the value of plan liabilities are lower on a mass withdrawal basis.

previous five years, (2) had no unfunded vested benefits for at least three of the previous five years, and (3) were projected to be fully funded and to have no unfunded vested benefits for the next four years.[47]

Concerns Raised by the Discussion Draft

If the provisions of the discussion draft were to be enacted, the following are some possible concerns that have been raised.

Adjustable Benefit Plans Currently Exist

One of the main features of the composite plans proposal is that participants' benefits could be adjusted based on the performance of investments in the plan. This would relieve employers in the plan from the obligation to increase contributions in response to investment losses. This feature is already available to an extent in a type of DB plan called an *adjustable benefit plan* or *variable defined benefit plan*.[48] In this type of plan, participants are guaranteed (1) a minimum (also called a floor) benefit that is calculated using conservative assumptions[49] plus (2) a variable benefit that can increase or decrease based on performance of the investments in the plan. A participant's benefit cannot be changed once payments begin in retirement.

The adjustable benefit plan differs from the composite plan proposal in several aspects: the plan would be responsible if there were insufficient assets from which to pay the floor benefits (as might occur if there were large investment losses); benefits would be insured by PBGC; the plan would continue to pay PBGC premiums; and employers would still be subject to withdrawal liability.

Several plans have adopted adjustable benefit plans, including a plan that covers workers in the United Food and Commercial Workers Union and a plan that covers workers in the Newspaper Guild of New York.[50]

Potential Consequences for Legacy and Composite Plan Funding

Funding for existing multiemployer plans would be lower under the provisions of the composite plan proposal. This is because a plan could amortize existing underfunding over 25 years (an

[47] It appears that the elimination of withdrawal liability would be permanent. For example, if a legacy plan that was able to eliminate withdrawal liability subsequently had unfunded vested benefits (such as would occur if the value of plan investments declined), then employers would be able to withdrawal from the legacy plan without having to pay for their share of unfunded benefits.

[48] The *Solutions Not Bailouts* plan presented by NCCMP (available at http://webiva-downton.s3.amazonaws.com/71/59/b/39/1/Solutions_Not_Bailouts.pdf) included a discussion of adjustable benefit plans in their section on "Innovation: New Structures to Foster Innovative Plan Designs." More information on adjustable benefit plans is available at https://www.cheiron.us/cheironHome/content/solutions/app/understanding-APP.

[49] For example, the plan could use a low discount rate to estimate the present value of future benefit obligations and have a relatively conservative investment strategy.

[50] See Kevin Olsen, *Adjustable pension plan design begins to gain converts*, Pensions and Investments, April 26, 2016, at http://www.pionline.com/article/20130429/PRINT/304299981/adjustable-pension-plan-design-begins-to-gain-converts.

increase from 15 years under current law).[51] All else being equal, each year's contribution to a legacy plan would be lower than under current law.[52]

For composite plans that are adopted as a component of an existing multiemployer plan, contributions would be allocated to the legacy plan based on the legacy plan's transition contribution rate. In addition, if a legacy plan were to enter critical or endangered status, required contributions to the legacy plan would likely increase. If this were to occur, the proposal contains a provision that the composite plan could not receive less than 25% of the combined contribution to the legacy and the composite plan. This requirement could lead to a worsening of the legacy plan's funded status if required contributions in the legacy plan were more than 75% of the combined contributions to the legacy and composite plan.

Withdrawal Liability in Legacy Plans

Under the composite plan proposal, the amount that employers would have to pay in withdrawal liability would likely decrease and could be permanently eliminated from a plan.

Under the composite plan proposal, an employer's withdrawal liability payments would likely decrease, even though there might not be any change in the total amount of an employer's withdrawal liability. One of the components in the calculation of withdrawal liability payments is the average of contributions in the 10 years prior to an employer's withdrawal.[53] In a multiemployer DB plan in which participants are earning benefits, employers' contributions go toward (1) new benefits earned by participants and (2) an amortized portion of unfunded benefits. However, employer contributions to a legacy would only go toward an amortized portion of unfunded benefits. The discussion draft contains a provision that excludes contributions to a composite plan from the calculations of withdrawal liability payments.

If a legacy plan were to become 100% funded (using PBGC's mass withdrawal assumptions), it would be permanently relieved of withdrawal liability. If the plan were to subsequently become underfunded, required employer contributions might increase in order to make up for the underfunding. However, employers would be able to exit the plan without paying withdrawal liability. If such a plan were to become insolvent, the financial assistance required from PBGC could be larger than it would be under current law.

Investment Policy in Composite Plans

A pension plan's investment policy determines the percentage of the plan's assets that are invested among several investment options, such as equities (stocks and bonds), fixed income (bonds), real estate, and alternative assets (such as private equity). In traditional DB plans, the employers who make the contributions to the plan bear the investment risk because their contributions would increase to make up for investment losses. In composite plans, participants would bear most of the investment risk because their benefits would decrease in response to investment losses.[54]

[51] This is sometimes referred to as a *fresh start* for multiemployer plan funding.

[52] Under current law, amortization period for losses in multiemployer plans is 15 years.

[53] See 29 U.S.C. §1399(c).

[54] Employers could also bear some investment risk. One item in the realignment program calls for *proposed* contribution increases. Contribution increases are not mandatory.

It is possible that the asset allocation appropriate for a composite plan could differ from the asset allocation for a DB plan.[55] If participants in composite plans had less tolerance for risk, then they might prefer an investment allocation that is weighted toward more conservative investments than is true in current DB plans.[56] Participants in DC plans bear investment risk and in most DC plans participants are able to choose their investment allocations from a range of investment options provided by the plan sponsor. In general, a pension plan's investment policy is established by the plan's investment policy committee. Participants in composite plans would have no direct influence in a composite plan's investment policy and the discussion draft does not contain any provisions regarding the investment policy of composite plans.

Realignment Program Concerns

Some have suggested that the realignment program that would be adopted if funding levels in a composite plan were to fall to below 120% of plan liabilities could be made clearer.[57] For example, the discussion draft (1) indicates that a realignment program *may* include certain measures to be undertaken (such as proposed employer contribution increases or a reduction in benefit accruals) and (2) contains three "tiers" of measures as part of the realignment program. However, the discussion draft only indicates that the measures in a given tier *may*—but does not require that they—be included in a realignment program. This potentially leaves plan trustees discretion about the adoption of the specific measures of a realignment program and participants uncertain about how their benefits would be affected by funding shortfalls.

Proposal Does Not Address Existing Multiemployer Plans Facing Insolvency

The discussion draft does not contain any provisions to assist multiemployer plans in critical or critical and declining status. PBGC has indicated that the multiemployer insurance program is likely to become insolvent by 2025, as a result of several very large multiemployer plans in critical and declining status becoming insolvent.[58]

Possible Adoption of Composite Plans

Existing multiemployer plans would not be required to adopt composite plans. However, some of the features of composite plans (such as fixed contributions, the absence of withdrawal liability and the payment of PBGC premiums) could be attractive, from an employer's point of view, and

[55] See, for example, this discussion of target benefit plans in Canada: Aon Hewitt, *Investments for the Target Benefit Plan*, January 18, 2015, at https://retirementandinvestmentblog.aon.com/getattachment/242ef259-eac2-4d4d-8f6d-77e2b652b555/TargetBenefitPlan-Guide4-Jan2015-EN.pdf.aspx.

[56] The asset allocations among DB pension plans in the United States with 1,000 or more participants in 2013 were 50.6% stock, 33.7% investment-grade debt, 3% high-yield debt, 9.8% in alternative investments, 27.% in real estate, and 0.2% in cash. See Canstantinjn W.A. Panis and Michael J. Brien, *Asset Allocations of Defined Benefit Plans*, U.S. Department of Labor, November 15, 2015, at https://www.dol.gov/sites/default/files/ebsa/researchers/analysis/retirement/assetallocationofdefinedbenefitpensionplans.pdf.

[57] See, for example, a comment letter from the Bipartisan Policy Center on the discussion draft available at http://cdn.bipartisanpolicy.org/wp-content/uploads/2016/11/BPC-Comments-Multiemployer-Pension-Modernization-Act.pdf.

[58] See Pension Benefit Guaranty Corporation, "PBGC Reports—Multiemployer Program Needs Substantial Premium Increases; Single-Employer Program Likely to Eliminate Deficit by 2025," press release, June 25, 2016, at http://www.pbgc.gov/news/press/releases/pr16-09.html.

some employers in multiemployer DB plans may desire that their plan sponsors adopt composite plans.

In addition, the composite plan proposal is limited to the sponsors of multiemployer pension plans. It is also possible that the sponsors of existing single-employer DB pension plans could seek approval to adopt the composite plan model.[59] However, employers that sponsor single-employer DB pension plans face few obstacles to freezing or terminating their DB pension plan and adopting DC plans.

Stakeholder Considerations

Stakeholders such as policy makers, Members of Congress, employers and unions that participate in multiemployer plans, and groups representing retirees have identified a number of benefits and drawbacks in the proposal for composite plans. Among other issues, these include benefits for employers, risks for participants, possible effects on PBGC, and funding for legacy and composite plans. The policy considerations for some of these stakeholders are summarized in **Table 1**.

Table 1. Multiemployer Composite Plans Proposal: Selected Stakeholder Considerations

Stakeholder	Considerations
Employers	Employers would contribute fixed amounts to the plans. Employer contributions would not necessarily increase in response to underfunding. Employers would not pay withdrawal liability if they leave a composite plan. Employers would not pay insurance premiums to PBGC.
Participants	Participants would receive monthly benefit payments for life, though the benefit amount is not certain. Participants' benefits would decrease if the projected value of a plan's assets were less than 120% of the value of the plan's liabilities. Participants' benefits could increase if the projected value of a plan's assets were more than 120% of the value of the plan's liabilities. Participants' benefits would not be insured by PBGC. Participants' benefits in legacy plans could be at risk if the funding of legacy plans were weakened.
Pension Benefit Guaranty Corporation (PBGC)	PBGC would not insure benefits in composite plans. PBGC insurance revenue from legacy plans would likely decrease as the number of participants in legacy plans were to decrease. PBGC claims could increase if the funding of legacy plans were weakened.

Source: Congressional Research Service.

[59] Although target benefits pensions in Canada are generally multiemployer plans, the providence of New Brunswick, has authorized a *shared-risk* pension, which has some features that are similar to the composite plan proposal. The shared-risk pension can be adopted as a single-employer pension plan. See Alicia H. Munnell and Steven A. Sass, *New Brunswick's New Shared Risk Pension Plan*, Center for Retirement Research at Boston College, July 2013, at http://crr.bc.edu/briefs/new-brunswicks-new-shared-risk-pension-plan/.

Considerations for Employers

Employer concerns with existing multiemployer plans include (1) uncertainty over future contribution increases and (2) withdrawal liability. These concerns may cause employers in multiemployer DB plans to consider leaving their DB plans and establishing DC plans. In addition, these concerns make it difficult for existing multiemployer DB plans to attract new employers to the plan.[60] The composite plan proposal addresses these concerns.

Certainty of Contributions

An employer's future contributions to a DB pension plan may unexpectedly increase as a result of investment losses or other decreases in a pension plan's funding ratio.[61] The composite plan proposal does not include mandatory employer contribution increases in the event of decreases to a plan's funding ratio. Employer contributions could remain fixed, which could be an attractive feature to prospective employers that might consider joining the plan. Investment losses and other changes that negatively affect a plan's funding ratio would be addressed by the realignment program which includes proposed but not mandatory contribution increases and mandatory benefit decreases.

Absence of Withdrawal Liability

Concerns about withdrawal liability might be a factor that deters employers from joining an existing multiemployer DB plan. When a plan has insufficient assets from which to pay 100% of promised benefits, employers that leave the plan are assessed an amount equal to their share of unfunded benefits. Withdrawal liability raises several concerns among employers: (1) the amount of the withdrawal liability can sometimes be very large, which might place a burden on the employers in the plan; and (2) the disclosure of withdrawal liability might prompt concerns among lenders and other creditors to a company, even for companies that have no intention of withdrawing from a plan.[62]

Employers would likely find the absence of withdrawal liability an attractive feature of composite plans.

Pension Benefit Guaranty Corporation Premiums

Plan sponsors that adopt composite plans would not pay per participant annual premiums to PBGC.

[60] See Testimony of Randy G. DeFrehn in U.S. Congress, House Committee on Education and the Workforce, Subcommittee on Health, Employment, Labor, and Pensions, *Discussion Draft to Modernize the Multiemployer Pensions*, September 22, 2016, at http://edworkforce.house.gov/uploadedfiles/testimony_defrehn_9.22.16.pdf.

[61] For example, if the mortality assumptions a plan uses changes (for example, if plan participants live longer than had been expected), then the plan's future benefit obligations would increase as a result of an increases in expected benefit payments to participants. This would cause the value of plan liabilities to increase.

[62] See, for example, James P. McElligott Jr., Taylor W. French, and Robert M. Cipolla, "Sun Capital Decision Threaten Lenders with Controlled Group Liability," *The Banking Law Journal*, June 2014, pp. 483-491.

Considerations for Participants

In a composite plan, participants would (1) not be subject to the longevity risk associated with DC plans, (2) be exposed to investment risk if the value of plan assets decreases, and (3) be exposed to other risks that might increase the value of plan liabilities.

Lifetime Income for Participants

One of the concerns with DC plans is that participants could spend all of their assets while alive and thus not have their DC account as a source of income for some of their retirement.[63] An April 2013 survey indicated that about 43% of U.S. investors were concerned with outliving their retirement savings.[64] Although participants in DC plans have options to purchase annuities (either in their plan, if that is an option, or separately from an insurance company), a June 2016 survey by TIAA (a large provider of annuities) found that only about 14% of individuals had purchased an annuity.[65] The composite plan proposal would provide monthly income in retirement for the life of the participant (and spouse, if married).

Pension Benefit Guaranty Corporation Insurance

Participants' benefits in composite plans would not be insured by PBGC. If the plan were to become insolvent and unable to pay benefits, PBGC would *not* provide financial assistance and participants would not receive their benefits.

Participants Benefits and Decreases in Plan Funding

Certain risks could negatively affect the value of plan liabilities, which would cause a plan's funding ratio to decrease. These risks include risks from investment losses and changes to the assumptions used to value plan liabilities.

Investment Risk

In most DB plans, the plan sponsors must increase their contributions to make up for investment and other losses that cause the plan's funding ratio to fall below 100%. In DC plans, plan participants bear investment losses through smaller account balances. Participants in DC plans could increase their contributions if their contributions are below the annual contribution limit, which in 2016 and 2017 is $18,000 per year ($24,000 if 50 years of age or older).[66] In composite plans, investment losses would be made up by a combination of proposed contribution increases and decreases in promised benefits. Unlike DB plans, there is no obligation for plan sponsors to increase contributions in the event of investment losses, and unlike DC plans, plan participants would be unable to make contributions to composite plans.

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[63] See, for example, James M. Poterba, Steven F. Venti, and David A. Wise, *The Drawdown of Personal Retirement Assets*, National Bureau of Economic Research (NBER), Working Paper no. 16675, January 2011, at http://www.dartmouth.edu/~bventi/Papers/w16675.pdf.

[64] See Dennis Jacobe, *Nonretired U.S. Investors Grow Optimistic, Retirees Don't*, Gallup, April 26, 2013, at http://www.gallup.com/poll/162038/nonretired-investors-grow-optimistic-retirees-don.aspx?.

[65] See TIAA, *TIAA 2016 Lifetime Income Survey: Executive Summary*, September 16, 2016, at https://www.tiaa.org/public/pdf/C33638_Lifetime_Income_ExecSummary.pdf.

[66] See Internal Revenue Service, "IRS Announces 2017 Pension Plan Limitations; 401(k) Contribution Limit Remains Unchanged at $18,000 for 2017," press release, October 27, 2016, at https://www.irs.gov/uac/newsroom/irs-announces-2017-pension-plan-limitations-401k-contribution-limit-remains-unchanged-at-18000-for-2017.

Other Risks

Plan liabilities (and a plan's funding ratio) would decrease under the following circumstances: (1) if plan participants were to live longer and mortality tables were revised to reflect an increase in life expectancy, then a plan's funding ratio would decrease; (2) if there were changes to the actuarial assumptions used by the plan,[67] or (3) employers were to withdraw from the legacy plan. For example, if the discount rate that plans use to calculate the present value of future benefit obligations were to decrease, then the value of future benefit obligations would increase. A composite plan might have to address these, or similar, changes to the value of plan liabilities with the realignment program, which could include proposed contribution increases and potentially mandatory benefit reductions.

Effect on Pension Benefit Guaranty Corporation

If the composite plan proposal were enacted, over time, PBGC would likely see its premium revenue decline.

Because composite plans would not be covered by PBGC insurance, the plans would not pay premiums to PBGC. PBGC would not have any liability for benefits in a composite plan. In addition, a composite plan would not become insolvent, because a plan in financial difficulty would be able to reduce participants' benefits to $0.

Although legacy plans would still be pay premiums to PBGC, PBGC's premium base would shrink. Over time, the number of participants in legacy plans would decline because (1) plan participants would die and (2) no new participants would receive benefits in the legacy plan. Lower premium revenue would leave PBGC with fewer resources from which to provide financial assistance to multiemployer plans.

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[67] Changes to a plan's actuarial assumptions could also decrease the value of plan liabilities.