



# COMPOSITE PLAN LEGISLATION JEOPARDIZES THE RETIREMENT SECURITY OF WORKERS AND RETIREES



**By the Trustees of the Western Conference of  
Teamsters Pension Trust**



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# COMPOSITE PLAN LEGISLATION JEOPARDIZES THE RETIREMENT SECURITY OF WORKERS AND RETIREES

Composite plan legislation, including the GROW Act, poses a grave threat to the retirement security of millions of Americans. The GROW Act runs directly counter to the goals of strengthening multiemployer plans and placing the Pension Benefit Guaranty Corporation (PBGC) multiemployer insurance program on solid fiscal ground. It has no place in multiemployer pension reform.

The GROW Act would allow plan trustees to siphon contributions from an existing plan to create a new composite plan that provides inferior benefits, leaving neither plan—the existing plan, nor the composite plan—with enough money to fulfill their pension promises. As a result, workers and retirees in both existing and composite plans are placed at risk of devastating benefit cuts, and the PBGC’s ability to insure multiemployer plan pensions is subjected to extraordinary damage. At the same time composite plans are likely to increase PBGC liabilities by reducing existing plans’ funding levels and enabling employers to leave an existing plan at substantially reduced cost, the legislation would drain funds from the PBGC multiemployer insurance program by exempting composite plans from paying PBGC premiums.

These risks to retirement security and the multiemployer plan system make the GROW Act’s inclusion in any multiemployer plan legislation a poison pill. This report, backed by an in-depth actuarial study,<sup>1</sup> illustrates the far-reaching damage of composite legislation to the funding of multiemployer plans, the solvency of the PBGC, and the benefit promises to millions of Americans.

## **The GROW Act starves plans of money needed to fulfill their pension promises**

The GROW Act permits the creation of two plans out of a single, finite pool of assets—leaving neither plan—the existing plan, nor the composite plan—with enough money to pay promised benefits. Under the legislation, multiemployer plan trustees may “refinance” their obligations to workers and retirees in an existing plan over 25 years instead of 15 years. As a result, the amount of money contributed to an existing plan is immediately reduced. Like refinancing a house with a new, longer-term mortgage, less money is contributed to the existing plan because the debt is paid off more slowly. The difference is siphoned off to fund the new composite plan.

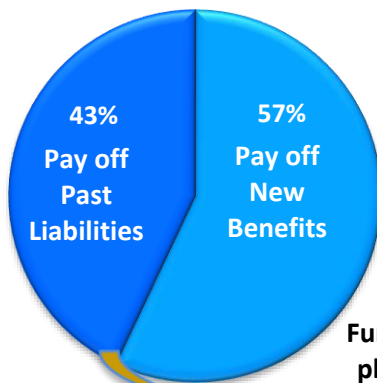
For a typical Green Zone plan that converts to a composite plan, the 25-year “fresh start” results in an immediate 20% reduction in funding to the existing plan. Prior to conversion to a composite plan, 43% of incoming contributions were set aside to pay off past liabilities and 57% was used to pay for new benefits. After conversion, the funding of the existing plan is reduced to 23% of incoming contributions, with 77% going to pay for new composite plan benefits. Yet, as shown below, despite this substantial reduction in existing plan funding that is siphoned to the new composite plan, the composite plan still lacks the money needed to fulfill its benefit promises.

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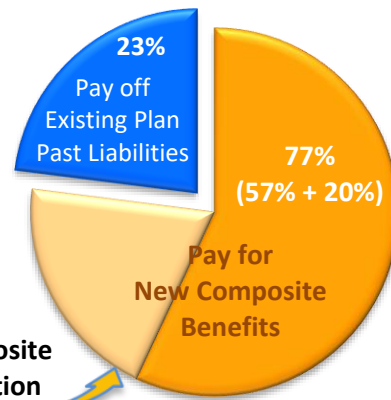
<sup>1</sup> See Appendix for a detailed description of the assumptions and methods used in this study.

## COMPOSITE PLAN LEGISLATION IMMEDIATELY REDUCES EXISTING MULTIEMPLOYER PLAN FUNDING AND DIVERTS THAT MONEY TO THE COMPOSITE PLAN

Existing Multiemployer Plan  
Contribution Allocation



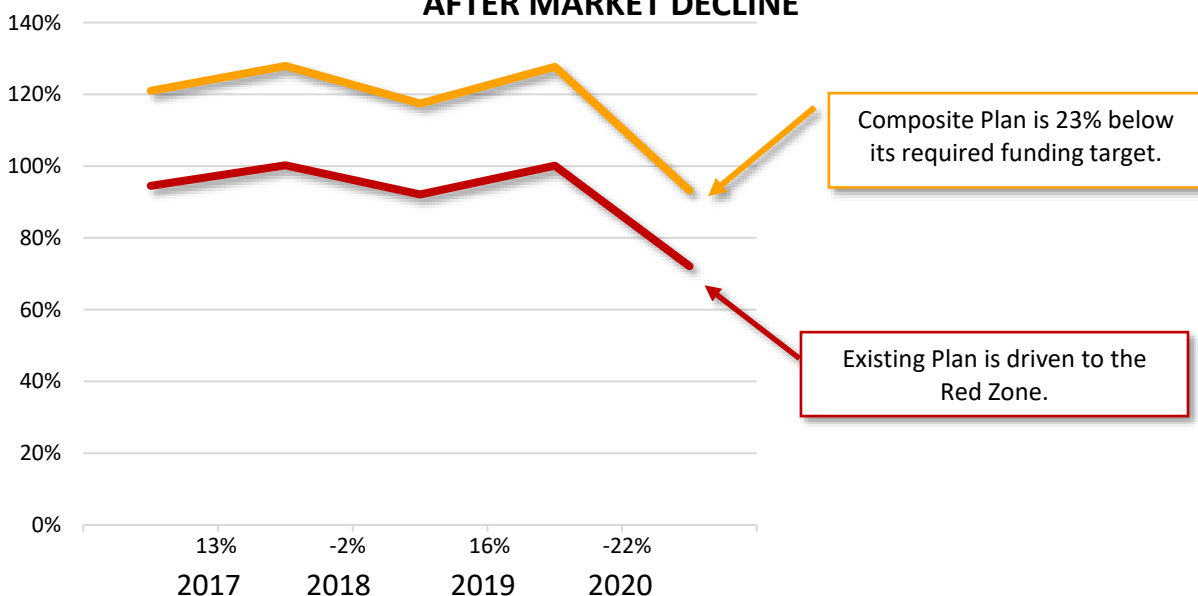
Existing / Composite Initial  
Contribution Split After Transition



Funding diverted to composite plan by "fresh start" election

With inadequate funding, both the existing plan and composite plan will be unable to endure investment market downturns of the kind seen in recent years—ones that should be expected to recur in the future. For example, investment returns similar to those in early 2020 caused by the novel coronavirus would drive a previously healthy existing plan to the Red Zone. At the same time, these investment returns would render a typical, mature composite plan 23% below its required funding target. In the absence of unrealistic contribution increases from employers, these funding shortfalls will result in substantial benefit cuts for participants in both the existing plan and the composite plan.

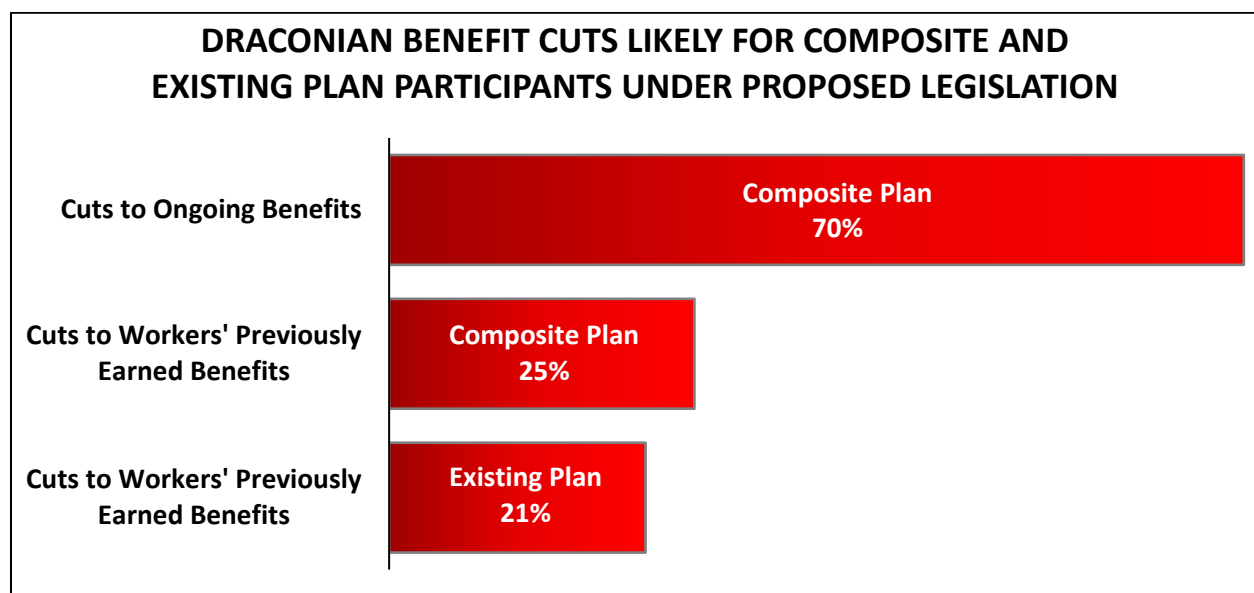
## GROW ACT PUTS PREVIOUSLY HEALTHY PLANS AT RISK AFTER MARKET DECLINE



This need for the existing and composite plans to break their pension promises stands in stark contrast to the experience of the same plan had it not converted to a composite plan. Under the same investment return scenario, that plan would remain in the Green Zone, allowing it to weather these negative investment returns without the need to cut workers' or retirees' benefits.

### **The GROW Act subjects workers and retirees to risk of draconian benefit cuts**

The GROW Act requires substantial benefit cuts as a result of economic downturns of the kind that have occurred recently and should be expected to reoccur. After the same investment returns described above, the composite plan would be required to cut workers' expected future benefits by 70% and previously earned benefits by 25%. At the same time, the existing plan must cut workers' previously earned benefits by 21%.



To avoid these benefit cuts, employers would be required to increase plan contributions by 82%—above and beyond what they've already committed. This is not a realistic option. Dramatic contribution increases are impracticable in any economic climate—and even more so during an economic downturn.

The GROW Act also puts retirees' benefits at risk of unprecedented cuts. Composite plan legislation permits cuts to retirees' benefits in the composite plan without even the few procedural protections for plan participants offered by the Multiemployer Pension Reform Act of 2014 (MPRA).<sup>2</sup>

<sup>2</sup> In general, MPRA permits retiree pension cuts after a process that requires the Treasury Department, in consultation with the PBGC and the Department of Labor, to determine whether a deeply troubled plan's application to cut benefits satisfies requirements set by Congress. If the Treasury Department determines that the plan's application meets these requirements, the benefit cuts are submitted to a vote of the plan's participants and beneficiaries of a plan. The Treasury Department can overturn a vote rejecting benefit cuts and require that they be imposed in certain circumstances.

This ability to make unprecedented and draconian benefit cuts may be insufficient to save the existing plan from insolvency. A severe economic downturn can put a previously healthy plan on a path to insolvency as a result of negative investment returns, a reduction in incoming contributions, and employer exodus from the plan<sup>3</sup>—all at precisely the time when the existing plan could most use the funds lost as a result of the 25-year fresh start. Moreover, the GROW Act caps the amount of contributions that the existing plan can receive by guaranteeing that at least 25% of incoming contributions go to the composite plan. Faced with this cap, the existing plan may be starved of funds it needs to remain solvent.

If the existing plan becomes insolvent, benefits must be cut to the level guaranteed by PBGC insurance. For many retirees, such cuts would be nothing short of catastrophic. Any retiree who worked 30 years for their benefit would have their pension reduced to \$12,870—the maximum insured amount guaranteed by the PBGC under current law—regardless of the amount of benefits that they earned. Making matters worse, benefits can be cut even lower if the PBGC’s multiemployer insurance program runs out of money. If that happens, retirees would lose nearly their entire pensions.



### **The GROW Act allows employers to leave existing plans without paying their share of the plans’ liabilities**

The GROW Act incentivizes employers to leave the multiemployer plan system altogether without meeting their obligations to ensure existing pension promises are funded. Under current law, an employer may withdraw from a multiemployer pension plan but must pay withdrawal liability to cover its share of the plan’s liabilities. How much an employer pays in yearly withdrawal penalties is calculated based on its contributions to the plan in the ten years up to the time of withdrawal.

The GROW Act would eliminate withdrawal liability for composite plans, and it can dramatically reduce the cost of withdrawing from an existing plan, leaving fewer employers to fund existing plan benefits. Under the GROW Act, contributions to the composite plan are disregarded for purposes of determining withdrawal liability. By allowing employers to drastically cut their contributions to the existing plan by refinancing through the 25-year fresh start, the amount of contributions to the existing plan declines significantly.

As a result, employers can withdraw from existing plans after a decade by making dramatically reduced withdrawal liability payments—payments that may be substantially below the withdrawing employers’ share of the plan’s liabilities. This imposes another drain on existing plan funding, placing workers and retirees at even greater risk of being subject to devastating benefit cuts and existing plans at greater risk of insolvency.

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<sup>3</sup> As discussed in the section below, the GROW Act can incentivize employers to leave the multiemployer plan system by allowing them to withdraw from existing plans after a decade with dramatically lower withdrawal liability payments.



## **The GROW Act deepens the current PBGC solvency crisis and risks a new one**

The GROW Act severely weakens the PBGC's ability to insure multiemployer plan benefits, exacerbating its current solvency crisis and risking a new one. The GROW Act likely will increase PBGC liabilities by reducing the cost of leaving plans and placing existing plan funding in jeopardy through the 25-year fresh start and the cap on the amount of contributions existing plans can receive.

At the same time, the GROW Act drains funds from the PBGC by exempting composite plans from paying PBGC premiums. Because the GROW Act requires that no new workers may participate in the existing plan, the number of participants in existing plans will sharply decline over time, resulting in a corresponding drastic reduction in PBGC funding.

## **Analysis published by proponents of the GROW Act ignores the harm it imposes and illustrates composite plans' threat to retirement security**

A recent "case study" published by Josh Shapiro of the Groom Law Group on behalf of proponents of the GROW Act purports to show the advantages of a composite plan but instead illustrates the dangers the GROW Act poses to Americans' retirement security. The study is deeply flawed because it ignores the impact that a composite plan would have on the existing plan—even though a composite plan cannot exist without one.

The Groom study excludes the existing plan from its analysis—disregarding the GROW Act's requirement that a composite plan must be connected to an existing plan. Had the existing plan been acknowledged, the study would have to contend with the damage caused by diverting funds from the existing plan to fund the composite plan. As shown above, without sufficient funding, the existing plan would be unable to experience expected economic downturns without requiring devastating benefit cuts or unrealistic employer contribution increases. Moreover, the same market volatility puts workers in the composite plan at risk of draconian benefit cuts.



Instead, the study models a traditional multiemployer plan with some "composite features"—but not an actual composite plan. Without support, the study imagines a multiemployer plan that is 15% better funded than a traditional multiemployer plan and that has ability permitted by the GROW Act (but not current law) to cut workers' and retirees' pensions. Unsurprisingly, the study concludes that after additional worker and retiree benefit cuts, this better funded plan would be in a better position to withstand a market downturn than the traditional multiemployer plan.

Though purporting to support composite plan legislation like the GROW Act, the Groom study actually illustrates the danger of composite plan legislation. As described above, a typical Green Zone plan that converts to a composite structure can expect an immediate 20% reduction in funding. Just as an imagined plan that is 15% better funded is in a better position going into a market downturn, a real multiemployer plan that has its funding raided by a new composite plan will be in a far worse position to weather investment declines without devastating benefit cuts.

The GROW Act jeopardizes the retirement security of millions of Americans. A case study that assumes away the grave risks of composite plan legislation does not alter this reality.

## **APPENDIX: ACTUARIAL STUDY ASSUMPTIONS AND METHODS**

This report reflects the findings of an actuarial study commissioned by the Western Conference of Teamsters Pension Plan. The assumptions and methods used in this study are described in this Appendix.

### **Traditional Defined Benefit Plan Assumptions**

The Traditional Defined Benefit Plan (“Traditional Plan”) is a plan that does not convert to the composite plan structure. It is also the starting point for the existing plan. As of the start of the study, the Traditional Plan had the following characteristics:

Funding as of the start of the study:

- Plan liabilities of \$275 million based on a 7% discount rate assumption, with the following liability allocation:
  - Approximately 30% for active participants, 10% for vested terminated participants, and 60% for participants in pay status
- Market Value of Assets of \$255 million and Actuarial Value of Assets of \$246 million
- Annual contributions of \$10 million
- Normal Cost of \$5.7 million (beginning of year) before operating expenses based on an annual benefit accrual of \$120 per month.
- Credit Balance of \$28 million
- Funded Status of approximately 93% on a market value of assets basis
- Initial annual operating expenses of \$650,000 increasing by 3.5% per year
  - Operating expenses added as annual load to Normal Cost
- Stable contribution base units
- Stable normal cost, net of expenses

### **Existing Plan Assumptions**

At transition to the composite plan structure, the existing plan is frozen. This Existing Plan is referred to as the “Legacy Plan” in the GROW Act. The Existing Plan has the same initial characteristics as the Traditional Plan. The following modifications are made to the Existing Plan as a result of the transition:

- Benefit accruals cease—commonly referred to as a “benefit freeze”
- The “25-Year Fresh Start” for minimum funding is elected
- Initial annual operating expenses remain at \$650,000 increasing by 3.5% per year
- The initial annual contributions is \$2.3 million based on the Transition Contribution Rate (TCR) equal to a 25-year amortization of unfunded liability on a market value of assets basis plus operating expenses. The TCR increases each year as the operating expenses increase.

- In order to cover the increase in the TCR due to operating expense increases, future contributions are reallocated from the Composite Plan to the Existing Plan.

### **Composite Plan Assumptions**

At transition, a Composite Plan is established with the same demographics as the Traditional Plan but no assets or liabilities. The demographic assumptions used to value the Composite Plan are the same as those of the Traditional Plan.

The following additional assumptions were used to project the Composite Plan funding:

- Based on the “25-year fresh start” in the Existing Plan, \$7.7 million is available for contributions to the Composite Plan.
  - This initial contribution level supports an annual benefit accrual of \$127 per month based on the requirement that the initial contribution equal at least operating expenses plus 120% of normal cost.
- Initial annual operating expenses of \$130,000 increasing by 3.5% per year
- Contributions to the Composite Plan are adjusted each year to the extent necessary to pay TCR in the Existing Plan.

### **Investment Return Assumptions**

Annual 7% net investment return for 10 years after transition

Market volatility period for years 11 through 14 as follows:

<u>Year</u>	<u>Actual Return</u>
11	13.00%
12	-2.00%
13	16.00%
14	-22.34%

Returns for years 11 through 13 are the approximate returns for the Western Conference of Teamsters Pension Plan. The return for year 14 is the median return for the multiemployer defined benefit plan universe from 2008.<sup>4</sup>

From February 19, 2020, through March 23, 2020, a portfolio composed of 45% U.S. equities, 20% international equities, and 35% U.S. fixed income is estimated to have returned -22.5%, similar to the median return for multiemployer defined benefit plans during 2008.

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<sup>4</sup> See Segal Consulting Composite & Legacy Plan Comparative Stress Testing (September 2016).



## Rehabilitation Plan/Realignment Program Assumptions

When determining the need for a rehabilitation plan or realignment program, future returns were assumed to be 7% annually, net of investment expenses.

To determine the contribution increases and/or benefit cuts necessary under the rehabilitation plan or realignment program, the following assumptions were used:

- Contribution rate increase calculations assume that additional contributions would not become effective until 1 year after the certification date and all contribution rate increases are applied to funding only; there are no additional benefit accruals tied to the increased contributions.
- Benefit cuts were estimated as the amount necessary to satisfy the rehabilitation plan or realignment program requirements as of 1 year after the certification date. Benefit cuts are expressed as a percentage of non-retired liability—that is, benefit cuts are applied to active and vested terminated participants.
  - Non-retired liabilities are assumed to make up 25% of the Existing Plan's total liability and 50% of the Composite Plan's total liability when the rehabilitation and realignment plans are implemented.
  - Such benefit cuts may not be allowable under Critical status rules for plans that do not have sufficiently large non-retired benefits. In that case, additional contributions and/or declaring "all reasonable measures" may be required.

Order and magnitude to contribution increases/benefit cuts:

The Traditional Plan remains in the Green Zone and does not require any action.

The Existing Plan would be certified as Critical (possibly Critical and Declining) and required to implement a rehabilitation plan after the market crash.

- The maximum contribution of \$7.5 million (75% of total \$10 million contribution) is assumed to be reallocated from Composite Plan. Additionally, previously earned non-retired benefit value is cut by 21%. This combination is required to prevent the plan from having an accumulated funding deficiency at the end of the rehabilitation period.

The Composite Plan, even before the reallocation of the contribution to the Existing Plan, would be projected to be 97% funded 15 years after the market crash. This is 23% behind the projected funding target of 120% within 15 years.

- After reallocating the maximum amount to the Existing Plan, \$2.5 million in contributions remain for the Composite Plan. In order to reach 120% funded in 15 years, the Composite Plan must reduce future accruals by 70% and cut previously earned non-retired benefit value by 25%.

In order to avoid benefit cuts in both the Existing Plan and the Composite Plan, additional contributions of \$8.2 million per year would be required. This would be allocated \$1.4 million to the Existing Plan and \$6.8 million to the Composite Plan.

Adjustments to rehabilitation/realignment plans beyond the above actions are beyond the scope of this analysis.