Proskauer

Significant Multiemployer and Single Employer Benefit Rule Changes Take Effect

January 20, 2015

On December 16, 2014, President Obama signed into law the $1.1 trillion Consolidated and Further Continuing Appropriations Act of 2015 (Appropriations Act), which includes some significant changes to the rules governing multiemployer pension plans, as well as a few changes affecting single employer pension plans. With respect to multiemployer plans, these changes were included in a division of the Appropriations Act called the Multiemployer Pension Reform Act of 2014, which, among other things, clarifies the Pension Protection Act of 2006 (PPA) funding rules applicable to multiemployer plans and also provides more troubled plans with new tools to avoid insolvency. While the most talked-about changes relate to plans in critical (the "red zone") or endangered (the "yellow zone") status, there are also a number of changes of which even well-funded multiemployer plans should be aware.

Key provisions from the law affecting multiemployer and single employer plans, which generally took effect January 1, 2015, are detailed below.

Changes to the Multiemployer Plan Funding Rules Generally:

- **Repeals the Sunset of PPA Rules.** A number of provisions of the PPA relating to funding (including the rules related to zone status and automatic five-year extensions of funding amortization periods) were set to expire as of December 31, 2014. With the signing of the Appropriations Act, the provisions are now set to remain in effect indefinitely.

Introduces the Option to Elect to Be in Critical Status. Under the Appropriations Act, for plan years beginning after December 31, 2014, a plan sponsor may elect, within 30 days after the actuarial zone status certification, to enter critical status even if the plan does not meet the normal critical status standards, as long as the plan actuary projects that it will do so in any of the succeeding five years. The purpose of this change is presumably to provide plans with the tools available in critical status (*e.g.*, reductions in adjustable benefits) to get a "head start" in taking remedial steps to improve the plan's funded status.

Notably, there are a number of additional notices and disclosures under this new rule. First, all annual actuarial zone status certifications will now need to state explicitly whether the plan is projected to be in critical status in the next five years. Second, if a plan makes this election, it must notify participants, beneficiaries, the bargaining parties, the Pension Benefit Guaranty Corporation (PBGC), and the Department of Labor (DOL). Third, the plan sponsor must notify the PBGC if it is projected to enter critical status in this five-year period but does not elect to be in critical status.

- **Clarifies the Rules for Emerging from Critical Status.** Previously, the criteria for *exiting* critical status differed from the criteria for *entering* critical status, resulting in a "revolving door" issue whereby a plan could exit critical status and immediately reenter it. The Appropriations Act addresses this issue, providing that plans can only emerge from critical status once the plan actuary certifies that the plan no longer possesses the characteristics of a critical status plan, and the plan is not projected to have an accumulated funding deficiency in any of the succeeding nine plan years.

Provides that Certain Endangered Status Plans are No Longer Considered to Be in Endangered Status. A plan in endangered status is required to establish a funding improvement plan that will result in its improving its underfunding by one third over a 10-year period. Over the last several years, there have been some plans that met the criteria for endangered status but did not require any changes to contributions or plan benefits in order to satisfy the requirement to improve their funded status. Under the PPA, these plans still had to endure the burdens of being in endangered status even though their funding improvement plan would require no action. Under the Appropriations Act, however, these types of plans are not considered in endangered status as long as they were not in critical or endangered status in the preceding year. If a plan would be in endangered status but for this legislative change, the plan sponsor must still notify the bargaining parties and the PBGC that the plan would be in endangered status without this exception.

- **Changes the Date an Endangered Status Plan's Target Funding Percentage is Calculated to the Time of Plan Certification.** As noted above, a funding improvement plan for a plan in endangered status must improve funding by one third of its underfunding over a 10-year period known as the funding improvement period. Under the PPA, the starting point for the funded percentage was measured as of the beginning of the funding improvement period. Under the Appropriations Act, however, it is now calculated as of the beginning of the plan year for which the plan is certified in endangered status. Using this earlier date removes uncertainty and also removes a possible disincentive to make plan changes before the funding improvement period begins.
- **Removes the Requirement that Funding Improvement Plans Avoid a Funding Deficiency Every Year.** Under the PPA, the funding improvement plan of a plan in endangered status was required to avoid a funding deficiency for every year in the funding improvement period. The Appropriations Act removed this requirement for plans in endangered status (although it appears that an excise tax would still apply if there is a funding deficiency when a plan is in endangered status).

Conforms the Restrictions for Endangered and Seriously Endangered Status Plans During Funding Plan Adoption and Funding Improvement Periods to Those for Critical Status Plans. Under the PPA, the restrictions applicable to endangered and critical status plans in their adoption periods and funding improvement/ rehabilitation periods differed to some extent. The Appropriations Act conformed these restrictions so that endangered status plans are now subject to the rules for critical status plans. Of note, this means that:

- Seriously endangered plans are no longer required to take reasonable actions during the adoption period to increase the plan's funded status and postpone accumulating funding deficiencies, and
- Once the funding improvement plan is adopted, endangered status plans are not prohibited from accepting a collective bargaining agreement (CBA) or participation agreement that (1) reduces the level of contributions for plan participants; (2) suspends contributions; or (3) excludes younger or newly hired employees from participation.

- **Clarifies the Contribution Schedule Applicable When Bargaining Parties Fail to Reach Agreement after First Conforming CBA.** The PPA provided for a default schedule where the bargaining parties did not adopt a funding improvement or rehabilitation plan schedule within 180 days after the existing CBA expires. However, this rule applied only to the expiration of the CBA in effect when the plan entered critical or endangered status and was silent as to subsequent CBAs. The Appropriations Act closes this gap, stating that if, 180 days after the expiration of a conforming CBA, the bargaining parties have not agreed to a contribution schedule, then the plan sponsor will implement the contribution schedule from the expired CBA (as updated).

- **Clarifies Adjustments That Are Disregarded for Withdrawal Liability Purposes.** Under the PPA, multiemployer plans in critical status had to disregard certain benefit reductions in determining the plan's unfunded vested benefits for withdrawal liability purposes. The Appropriations Act clarified the types of benefit reductions that are disregarded (including those related to benefit suspensions for plans in critical and declining status – discussed below – as long as the withdrawal occurred within 10 years of the suspension).

In addition, the PPA provided that critical status surcharges (applicable to employers prior to their adoption of a rehabilitation plan schedule) are generally disregarded in determining the unfunded vested benefits applicable to an employer. The Appropriations Act clarified that surcharges are also disregarded in determining the amount of an employer's annual payment. This rule applies to surcharges that accrue for periods on or after December 31, 2014.

Moreover, contribution increases that are either required or were made to enable the plan to meet the plan's funding improvement or rehabilitation plan will be disregarded for both allocation of unfunded vested benefits and the amount of the annual payment. This rule relating to disregarding contribution increases ceases to apply after the expiration of the CBA in effect when the plan emerges from endangered or critical status (except for purposes of calculating the highest contribution rate for plan years when the plan was in endangered or critical status). The rule is effective for contribution increases that go into effect on or after the first plan year beginning after December 31, 2014. The purpose of the rule appears to be to reduce the incentive for employers to withdraw prior to increases going into effect.

Changes Impacting Multiemployer Plans with More Significant Funding Issues:

Allows Insolvent and/or Terminated Plans to Pay Qualified Preretirement Survivor Annuities (QPSAs). Prior to the Appropriations Act, QPSAs were considered forfeitable benefits where the participant was still alive at the time a multiemployer plan became insolvent or terminated. As a result, under PBGC rules, an insolvent or terminated multiemployer plan with assets not sufficient to pay all nonforfeitable benefits was not permitted to pay a QPSA to the surviving spouse of any participant who died after the plan became insolvent or terminated. Under the Appropriations Act, QPSAs are not to be treated as forfeitable benefits solely because the participant is still alive at the time of plan insolvency or termination. Thus, QPSAs can now be paid with respect to participants who die after the date of plan insolvency or termination. Significantly, this change is effective retroactively for QPSAs becoming payable on or after January 1, 1985, as long as the surviving spouse did not die before December 16, 2014 (the date of the Appropriation Act's enactment). This retroactivity does create some practical questions about the payment of a QPSA that otherwise would have commenced many years prior, including how to adjust the payment amounts given the late commencement, and where the payments are otherwise past the required beginning date. Also, note, this change does not apply to other death benefits that are still considered forfeitable and therefore not payable after insolvency or termination, including certain lump sum death benefits.

- **Allows for the Suspension of Benefits of Certain Participants of Plans in "Critical and Declining Status".** The Appropriations Act creates an exception to the anti-cutback rules of ERISA and the Internal Revenue Code to allow, under certain conditions, plan sponsors of plans in "critical and declining status" to suspend (temporarily or permanently) benefits already earned by participants, including those already in pay status. The purpose of these new rules appears to be to allow trustees an opportunity to save their deeply troubled plans that would otherwise be headed toward short-term insolvency by making more modest benefit suspensions early, instead of waiting for insolvency and facing more severe cuts at the hands of the government agencies.

Each year, the actuarial certification for a plan must include a statement as to whether a plan is, or is projected to be, in critical and declining status for the plan year. Annual funding notices must include this information and, for plans in critical and declining status, additional information regarding the plan's projected insolvency and the possibility of benefit reductions. To qualify as a plan in critical and declining status, the plan must meet the requirements to be in critical status, and must be projected to be insolvent either in the current plan year or the succeeding 14 plan years (the succeeding 19 plan years if the plan's ratio of inactive to active participants is greater than 2:1 or the funding status of the plan is less than 80%).

Once a plan is determined to be in critical and declining status, certain requirements must be met in connection with any suspension of benefits, including the following:

- The plan actuary must certify that the suspensions are projected to allow the plan to avoid insolvency.
- The plan sponsor must have a written record that it is projected to become insolvent (absent the suspension) despite its having taken (and continuing to take) all reasonable measures to avoid insolvency. The Appropriations Act contains a number of factors to be taken into account in making this determination.
- The plan sponsor must apply for IRS approval. The IRS must approve or deny the application for suspension of benefits within 225 days of receipt of the application. If approved, the suspensions are then subject to a vote of the plan participants and beneficiaries, which is generally administered by the IRS (although the plan sponsor must prepare the ballot subject to certain content requirements in the law). Unless the majority of all plan participants and beneficiaries vote no, then the benefit suspensions will take place. Even if there is a negative vote, the IRS (after consulting with the PBGC and the DOL) may permit the suspension in the case of a "systematically important plan", as defined in the Appropriations Act.
- Concurrent with its application to the IRS, the plan sponsor must provide notice of the proposed suspension to plan participants and beneficiaries, labor organizations representing plan participants, and employers with an obligation to contribute to the plan.

In addition, certain plans with at least 10,000 participants must appoint (and pay the reasonable costs of) a retiree representative who will advocate for the interests of retired and deferred vested participants.

There are certain limitations on benefit suspensions, including the following:

- Monthly benefits cannot be suspended below 110% of the monthly amount guaranteed by the PBGC for each participant.
- Benefits cannot be suspended for those receiving benefits on account of disability.
- Benefits cannot be suspended for those who are at least 80 years old. (There is also partial protection for those between 75 and 80 years old.)
- Benefits can be suspended only to the extent reasonably estimated to achieve (but not materially exceed) the level necessary to avoid insolvency.
- Suspensions must be equitably distributed among the population. The Appropriations Act includes factors that may be taken into account in that regard.
- There are specific rules as to how post-suspension benefit improvements must be implemented.
- **Allows for PBGC-Facilitated Plan Mergers in Specified Situations.** The Appropriations Act provides specific authority for the PBGC to facilitate multiemployer plan mergers where the merger is in the interests of the participants and beneficiaries of at least one of the plans and is not reasonably expected to be adverse to the overall interests of the participants and beneficiaries of any of the plans. Assistance can include training, technical assistance, mediation, stakeholder communication and support relative to requests of other government agencies. The facilitation can include financial assistance if the following conditions are satisfied:
- At least one of the affected plans is in critical and declining status;
- The PBGC reasonably expects that the financial assistance provided will decrease the PBGC's anticipated long-term losses regarding these plans, and this action is necessary for the merged plan's solvency;
- The PBGC certifies to Congress that it will still be able to meet its current financial assistance obligations despite this assistance; and
- The financial assistance is paid exclusively from the PBGC multiemployer plan fund.

- **Expands the PBGC's Authority to Partition Plans.** Prior to the Appropriations Act, plans were only eligible for PBGC-facilitated partition when there was a substantial reduction in contributions as a result of an employer (or employers) being in bankruptcy. In those cases, only the liability associated with the service of the bankrupt employer(s) could be severed. Under the Appropriations Act, however, the bankruptcy of employers is no longer relevant. Now, the PBGC can order a plan partition if the plan sponsor requests PBGC assistance (and notifies participants of that request) and the following are satisfied:

- The affected plan is in critical and declining status;
- The PBGC determines that the plan sponsor has taken, or is currently taking, all reasonable steps to avoid insolvency (including by making the maximum amount of benefit suspensions);
- The PBGC reasonably expects that the financial assistance provided will decrease the PBGC's anticipated long-term losses regarding the plans, and that this action is necessary for the plan's solvency;
- The PBGC certifies to Congress that it will still be able to meet its current financial assistance obligations despite this partition; and
- The cost of the partition is paid exclusively from the PBGC multiemployer plan fund.

Where a plan is partitioned, a new plan (with the same sponsor and administrator as the existing plan) is created that has the minimum amount of plan liabilities necessary for the existing plan to remain solvent. The existing plan must pay the new plan the portion of the monthly benefit that exceeds the PBGC guarantee. There are special rules for the calculation of withdrawal liability, which generally depend on whether the employer withdraws within 10 years of the partition.

- **Repeals Reorganization Rules and Replaces Them with Rules for Critical Status Plans.** Under prior law, plans with funding issues were occasionally considered to be in "reorganization status", and were subject to specific enumerated requirements, if the plan met certain criteria similar, but not identical, to the triggers for critical status. The Appropriations Act repealed the reorganization rules and replaced these with the rules for critical status plans. This change avoids the confusion of subjecting plans in similar situations to different requirements.

The Appropriations Act also expanded the required scope of notice of impending insolvency to include the PBGC, and not simply the plan participants and beneficiaries, employers with an obligation to contribute to the plan, and labor organizations representing plan participants and beneficiaries. This expansion provides for further inclusion of government agencies in the status of plans with severe funding issues.

Other Changes Impacting Multiemployer Plans:

- **Adds Additional Plan Information Required to Be Disclosed and Retained.** Section 101(k) of ERISA requires multiemployer plans to provide certain information to participants, beneficiaries, employee representatives and contributing employers upon written request. In addition, Section 101(l) of ERISA requires multiemployer plans to furnish estimates of withdrawal liability to contributing employers upon written request.

The Appropriations Act modified these rules by providing a cause of action for employee representatives and employers who do not receive the requested information.

In addition, it added the following to the list of documents that must be disclosed under Section 101(k):

- Current plan document and amendments;
- Most recent summary plan description;
- Current trust agreement and amendments;
- An employer's participation agreement relating to the current plan year or any of the preceding five plan years (only required in response to that employer's request);
- Form 5500 for any plan year;
- Annual funding notice for any plan year;
- Audited financial statements for any plan year; and
- The most recent funding improvement plan or rehabilitation plan for plans in endangered or critical status, and the accompanying contribution schedules (other than a schedule applicable to a specific employer).

A number of these disclosures are now limited by statute to the last six years of information. Further, the Appropriations Act added much of this information to the record retention requirement of Section 107 of ERISA.

- **Increases PBGC Premiums for Multiemployer Plans from $13 to $26 Per Participant.** For plan years beginning after December 31, 2014, the PBGC premiums per participant have been increased from $13 to $26, and will then be adjusted for inflation and indexed annually. In addition, the PBGC must report to Congress by June 1, 2016 whether these increased premiums are projected to cover the PBGC's obligations for the upcoming 10- and 20-year periods. If the PBGC concludes that the resulting sums will not be sufficient, it must suggest revised premium amounts sufficient to meet the obligations.
- **Exempts Withdrawal Liability Settlements from Prohibited Transaction Rules.** The Appropriations Act clarifies that "any arrangement relating to withdrawal liability involving the plan", which would appear to include settlements of withdrawal liability claims against former contributing employers, are not subject to the prohibited transaction rules prohibiting party-in-interest transactions (although they are still subject to the self-dealing prohibitions).

Important Changes and Resulting Implications for Single Employer Plans:

- **Expands the Permissible Definition of Normal Retirement Age for Certain Defined Benefit Plans.** The Appropriations Act also addressed an issue arising from the IRS's 2007 guidance stating that plans must have a normal retirement age of at least age 62. Specifically, it provides that defined benefit plans will not be treated as failing the normal retirement age requirements if they defined normal retirement as the earlier of a permissible age or the age at which a participant completes the number of years (not less than 30) of service. Plans are allowed to amend their normal retirement age language to include the above approved language moving forward, but only for individuals who were plan participants (or employees of the employer) on or before January 1, 2017.

Updates the Rules Surrounding a "Substantial Cessation of Operations" Under ERISA Section 4062(e). When an employer who maintains a single employer plan substantially ceases operations (called a "4062(e) event"), the employer can be subject to a liability that equals the plan's unfunded benefit liabilities (measured on a termination basis) at the time of the 4062(e) event times the percentage reduction in active plan participants. After years of controversy surrounding its application, significant changes were made to this rule as follows:

- Section 4062(e) previously provided that an employer was considered to substantially cease operations if more than 20% of the *plan participants* were "separated from employment". The Appropriations Act reduces the percentage of the applicable workforce reduction that triggers a substantial cessation of operations from 20% to 15%, and now relates to the separation from employment of *all eligible employees (in any pension benefit plan of the employer, which would include employees in a 401(k) plan for this purpose)*, not simply the affected defined benefit plan's participants.
- There are a number of important exclusions and inclusions to the calculations of the number of participants terminated. For example, certain employee terminations can be excluded from this calculation if those employees are replaced "within a reasonable time" by an employee who is a U.S. citizen or resident. In addition, in an asset or stock sale, termination of an eligible employee is not counted where a new employer continues the operation, continues to employ the eligible employee and maintains a pension plan that includes assets and liabilities attributable to the employee's benefit (or the employee was not a participant in a pension plan). In such a disposition, the termination is also not counted if that new employer continues the operation, replaces the terminated employee and maintains a pension plan that includes the assets and liabilities attributable to the employee's benefit in the pension plan (if any).
- There is also a three-year lookback period that aggregates terminations that are related to the permanent cessation of operations.

The Appropriations Act also provides exemptions to the above rules regarding the treatment of employee terminations as substantial cessations of operations (including the notice requirements) when a plan is more than 90% funded or has less than 100 participants.

- Consistent with the PBGC's past practice, employers are now statutorily permitted to elect to satisfy the 4062(e) liability by making (generally over seven years) additional funding contributions to the affected plan. The new legislation also establishes that the PBGC cannot use funds allotted by this legislation to take action in connection with 4062(e) events.
- Finally, and perhaps most notably for large employers, the Appropriations Act directs the PBGC not to initiate any new enforcement action with respect to section 4062(e) that is inconsistent with its enforcement policy in effect on June 1, 2014. The PBGC implemented a 4062(e) Enforcement Pilot Program in 2012 under which the PBGC generally will take no action to enforce section 4062(e) liability against "creditworthy" companies or small plans with 100 participants or less. As a result, it appears that qualifying employers and plans will remain exempt from 4062(e) liability altogether.

The PBGC announced last week that, in light of the Appropriations Act, the PBGC will not be extending its self-imposed moratorium on the enforcement of Section 4062(e), which expired on December 31.

The Appropriations Act contains both minor improvements and significant changes to existing law of which all contributing employers to multiemployer plans and sponsors of defined benefit plans should be aware. The foregoing is intended to be a general summary of the significant changes present in the Appropriations Act relevant to both multiemployer and single employer plans, and is not intended to be an exhaustive review of the provisions thereunder. If you have any questions regarding the Appropriations Act and recommendations for effective compliance, please feel free to contact any of the Proskauer lawyers listed in this alert.

Related Professionals

- **Justin S. Alex**

Partner

- **Ira M. Golub**
- **Robert M. Projansky**
  Partner