Proskauer

PBGC Proposes Simplified Methods for Withdrawal Liability Calculations

March 29, 2019

On February 6, 2019, the Pension Benefit Guaranty Corporation ("PBGC") issued a proposed rule that impacts how multiemployer pension plans in endangered or critical status calculate withdrawal liability. The rule is not yet effective and remains subject to change. The PBGC will accept public comments on the proposed rule until April 8, 2019.

The proposed rule contains amendments to implement the statutory requirements of the Pension Protection Act of 2006 ("PPA") and the Multiemployer Pension Reform Act of 2014 ("MPRA"), which provide that benefit reductions, benefit suspensions, surcharges, and contribution increases under a funding improvement or rehabilitation plan must be disregarded when determining a withdrawing employer's total withdrawal liability and withdrawal liability payment amount (the "disregard rules").

The proposed rule also provides optional simplified withdrawal liability calculation methods for applying the disregard rules in determining withdrawal liability and annual payment amounts. Some of the simplified methods provided in the proposed rule are new and some are consistent with previous sub-regulatory guidance, such as PBGC Technical Update 10-3.

Key provisions from the proposed regulation are detailed below.

Adjustable Benefit Reductions and MPRA Benefit Suspensions

Under PPA, multiemployer plans in critical status must disregard the reduction or elimination of adjustable benefits ("adjustable benefit reductions") in determining unfunded vested benefits. In addition, multiemployer plans in critical and declining status that implement the benefit suspensions permitted by MPRA must disregard those suspensions in determining unfunded vested benefits for the 10-year period after the benefit suspensions become effective.

The proposed rule provides optional simplified methods for plans to disregard adjustable benefit reductions and MPRA benefit suspensions.

Using the simplified framework, a plan would first calculate an employer's withdrawal liability using the plan's withdrawal liability method and taking into account any adjustable benefit reductions and benefit suspensions. The plan would then add to the employer's withdrawal liability the employer's proportional share of the value of any adjustable benefit reductions or MPRA benefit suspensions. The proposed rule includes three simplified methods for the second step: one applies to adjustable benefit reductions and two apply to MPRA benefit suspensions.

- **Adjustable Benefit Reductions**. The proposed rule incorporates the guidance provided in PBGC Technical Update 10-3 for calculating an employer's proportional share of the value of any adjustable benefit reductions. The method applies for any withdrawal that occurs in any plan year following the plan year in which an adjustable benefit reduction takes effect and before the value of the adjustable benefit reduction is fully amortized.

For purposes of this calculation, the value of the adjustable benefit reduction as of a given plan year is the value of the reduced benefits as of the end of the year in which the reductions took effect, determined using the same assumptions to determine unfunded vested benefits under ERISA Section 4211, reduced as if that amount were being fully amortized in level annual installments over 15 years at the plan's valuation interest rate beginning with the first plan year after the plan year in which the benefits were reduced.

Using this method, an employer's proportional share of the value of an adjustable benefit reduction is determined by multiplying the value of the benefit reduction, as determined using the process explained above, by a fraction, the numerator of which is the amount of the employer's required contributions over the 5-year period prior to the withdrawal and the denominator of which is the amount of all employers' contributions over the same 5-year period (subject to certain adjustments, the "allocation fraction").

Technical Update 10-3 provides an additional adjustment for plans using the rolling-5 method, but the PBGC stated that it purposely decided to exclude it from the proposed rule to avoid ambiguity that might have required additional calculations and recordkeeping.

- **MPRA Benefit Suspensions**: The proposed rule provides two simplified methods for calculating a withdrawing employer's proportional share of the value of a MPRA benefit suspension: the static value method and the adjusted value method. Both methods apply for any employer withdrawal that occurs within the 10 plan years

after the end of the plan year in which a plan's MPRA benefit suspensions become effective.

- *Static Value Method.* Under the static value method, the present value of the suspended benefits as of a single calculation date would be used for all withdrawals in the 10-year period referenced above. The calculation date is either the effective date of the MPRA benefit suspension or the last day of the plan year in which the suspension becomes effective.[1]
- *Adjusted Value Method.* Under the adjusted value method, the present value of the suspended benefits for a withdrawal in the first year in the 10-year period referenced above is the same as the amount determined under the static value method. For years two through ten, the value of the suspended benefits would be equal to the present value of the benefits not expected to be paid in the year of withdrawal or thereafter due to the MPRA benefit suspension (determined as of the last day of the plan year before the employer's withdrawal).

With either method, the employer's proportional share of the value of a MPRA benefit suspension would equal the value of the benefit suspension multiplied by the allocation fraction, subject to certain adjustments. In addition, in the case of a plan using the static value method, the 5-year lookback period for determining the allocation fraction would be based on the five plan years ending before the plan year in which the benefit suspension becomes effective.

Contribution Increases

PPA requires plans to disregard employer surcharges in determining unfunded vested benefits. MPRA expanded the foregoing rule to also disregard employer surcharges for determining the employer's highest contribution rate for withdrawal liability payment calculation purposes.

MPRA requires plans to disregard contribution increases that are required or made under a funding improvement plan or rehabilitation plan from the contribution amounts of a withdrawing employer that are used to determine the employer's allocable share of the plan's unfunded vested benefits and to determine an employer's highest contribution rate for withdrawal liability payment calculation purposes. However, there is an exception if the increases are due to increased levels of work, employment, or periods for which compensation is provided or used to provide an increase in benefits. MPRA's changes apply to contribution increases that went into effect in plan years beginning after December 31, 2014, and to surcharges for which the obligation accrues on or after December 31, 2014.

After MPRA's enactment, certain underfunded plans have continued to take some contribution increases required by a funding improvement or rehabilitation plan into account for withdrawal liability purposes to the extent that the contribution increases result in higher benefit accruals for plan participants. These plans have reasoned that the increases are not solely required by the funding improvement or rehabilitation plan because the increases are counted toward benefit accruals. This position is supported by the proposed rule, which seeks to clarify that the portion of any contribution increases that increase benefit accruals as an integral part of the benefit formula (referred to in the preamble as "benefit bearing increases") are taken into account for calculating withdrawal liability. If finalized, this aspect of the proposed rule would have significant implications for underfunded plans with benefit accrual formulas that are tied to contribution amounts.

For those contribution increases which are required to be disregarded, the proposed regulation provides simplified methods for meeting this requirement when determining an employer's withdrawal liability allocation fraction, with one simplified method for determining the numerator (*i.e.*, the employer's contributions) and a choice between two simplified methods for determining the denominator (*i.e.*, the total contributions by all employers).

- **Simplified method for determining the numerator**. A plan using this method determines the numerator based on the withdrawing employer's contribution rate as of the last day of each plan year. The plan would first start with the employer's contribution rate as of the "freeze date," which is December 31, 2014 for a calendar year plan and the last day of the first plan year that ends after December 31, 2014

for any other plan. If the plan has a contribution rate increase after the freeze date that provides an increase in benefits, the rate increase is added to the contribution rate for each year to which the increase applies. The product of the employer's contribution rate on the freeze date (adjusted to reflect the foregoing increase(s) as appropriate) and the employer's contribution base units forms the numerator of the allocation fraction. A comparable amount determined for all employers would then be used for the denominator unless the plan uses the "proxy group method" for determining the denominator as described below.

- **Simplified methods for determining the denominator**. As noted above, the proposed rule allows a plan to use the same principles as the simplified method for determining a specific employer's numerator to determine the contributions by all employers for the denominator. Alternatively, the plan can use the "proxy group method."

Under the proxy group method, a plan must determine "adjusted contributions," which is the amount of contributions that would have been made excluding contribution rate increases that must be disregarded for withdrawal liability purposes, based on the exclusion that would apply for a representative "proxy" group of employers, rather than performing calculations for each of the employers in the plan.

To use the proxy group method, those employers that have a similar history of both total rate increases and disregarded rate increases ("rate schedule groups") must be identified. A proxy group must then be selected that together accounts for at least 10% of active participants and includes at least one employer from each rate schedule group, except that the proxy group does not need to include a member of a rate schedule group that represents less than 5% of active participants.

The plan would then need to determine the adjusted contributions for each employer in the proxy group by multiplying each employer's contribution base units for the plan year by what would have been the employer's contribution rate excluding the contribution rate increases that are disregarded in determining withdrawal liability. Next, adjusted contributions for each rate schedule group represented by the proxy group would be calculated by first determining the sum of the adjusted contributions for the proxy group members within a rate schedule group divided by the sum of those employer's actual contributions for the plan year. This results in an adjustment factor for that rate schedule group for the year. This adjustment factor is then multiplied by the contributions for the year by all employers, whether in the proxy group or not, in the same rate schedule group to determine adjusted contributions for the rate schedule group for the year.

Finally, the same steps would be performed to determine adjusted contributions at the plan level in order to determine that amount of total employer contributions to be used as the denominator of the allocation fraction. To do this, the sum of the adjusted contributions for all the rate schedule groups represented in the proxy group is divided by the sum of the actual contributions for the employers in those rate schedule groups, and the resulting adjustment factor for the plan is multiplied by the plan's total contributions for the plan year.

Calculating Withdrawal Liability after Plan Exits Endangered or Critical Status

Once a plan exits endangered or critical status, the disregard rules for contribution increases change. Specifically, in determining the allocation fraction a plan sponsor is required to include contribution increases (previously disregarded) as of the expiration date of the CBA in effect when a plan is no longer in endangered or critical status. However, contribution increases continue to be disregarded in determining an employer's highest contribution rate for withdrawal liability payment calculations. The proposed rule includes simplified methods to comply with the foregoing requirements, as described below.

- **Including contribution increases after a CBA has expired**. Because the determination as to whether contribution increases which occur after a plan has returned to the green zone should be included or disregarded for purposes of calculating withdrawal liability is dependent in part on when a CBA expires, the proposed rule provides two alternative simplified methods for determining which

contribution increases should be included and which should be disregarded for purposes of determining total employer contributions.

Under the first simplified method, all contribution increases occurring after the expiration date of the first CBA that expires after the plan's return to the green zone would be included in determining total employer contributions. Under the second simplified method, contribution increases previously disregarded would be included in calculating withdrawal liability for any employer withdrawal that occurs after the first full plan year after a plan is no longer in endangered or critical status, or if later, the plan year including the expiration date of the CBA requiring plan contributions that expires after the plan's return to the green zone.

- **Disregarding contribution increases applied while the plan was in endangered or critical status**. As noted above, a plan is required to continue to disregard contribution increases made while a plan was in endangered or critical status for purposes of calculating an employer's highest contribution rate even after it emerges from endangered or critical status. Because an employer's highest contribution rate is determined over a 10-year period, applying this rule would require a year-by-year determination of whether contribution increases should be included or disregarded. The proposed rule provides a simplified method to avoid this issue, which provides that a plan can provide that the highest contribution is the greater of
    - an employer's contribution rate in effect, as of December 31, 2014 (or the last day of the plan year that ends after December 31, 2014 for non-calendar year plans), plus any contribution increases occurring after that date and before the employer's withdrawal that must be included in determining the highest contribution rate under section 305(g)(3) of ERISA, or
    - the highest contribution rate for any plan year after the plan year that includes the expiration date of the CBA of the withdrawing employer that expires after the plan's return to the green zone, or, if earlier, the date as of which the withdrawing employer renegotiated a contribution rate effective after a plan's return to the green zone.

* * *

While the proposed rule is not yet effective, multiemployer pension plans and their contributing employers alike should consider the potential impact of these simplified methods on withdrawal liability calculations. Importantly, the simplified methods are optional and plans could continue to use alternative methods that are not specified in the PBGC's regulations. As noted above, the PBGC is accepting public comments on the proposed regulation through April 8, 2019. We will continue to monitor the proposed rule. Please feel free to contact us with any questions in the meantime.

[1] Additional adjustments would apply in the case of temporary MPRA benefit suspensions.

Related Professionals

- **Ira M. Golub**
- **Robert M. Projansky**
  Partner
- **Anthony S. Cacace**
  Partner
- **Justin S. Alex**
  Partner