Recommendations to the Congress for Revising Multiemployer Plan Termination Insurance

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INTRODUCTION

On July 1, 1978, the PBGC issued a comprehensive analysis of the current statutory multiemployer plan termination insurance program and its potential effects on plan participants, contributing employers, and the growth and continuance of multiemployer plans. 1/ That report, which was required by Public Law 95-214, contained options for addressing the problems of multiemployer plan termination insurance but did not set forth specific recommendations. 2/ This paper sets forth PBGC's recommendations for revising ERISA as it relates to termination insurance for multiemployer pension plans and certain ongoing operations of such plans.

The pension plan termination insurance program, which covers private defined benefit plans, was enacted by Congress to protect employees and former employees against loss of pensions in the event their plans were to terminate with insufficient funds to pay the pensions earned under the plan.

There are two broad categories of pension plans: defined benefit plans and individual account or defined contribution plans. Defined benefit plans are covered by termination insurance, while individual account or defined contribution plans are not.

A defined benefit plan is a pension plan other than an individual account plan and, generally, is one that provides a definite benefit for each employee upon retirement (usually expressed as $X for each year of service or as a percentage of earnings). Contributions in such a plan are intended to be sufficient, on the basis of actuarial assumptions on such factors as interest, mortality, and turnover, to fully pay the benefits when due. However, participants are entitled to the definite benefit, without regard to the money actually contributed to that plan, so that if the plan were to terminate with insufficient assets to pay all the promised benefits, participants could lose benefits to which they are entitled under the plan's provisions. Termination insurance provides protection against such benefit losses.

1/ Multiemployer Study Required by P.L. 95-214, PBGC, July 1, 1978.

2/ Public Law 95-214 required the PBGC to study the financial problems relating to mandatory termination insurance coverage of multiemployer pension plans under Title IV of the Employee Retirement Income Security Act of 1974 (ERISA) and to report to the Congress on actions which might be taken to solve these problems.

In an individual account or defined contribution plan, a definite benefit is not established. Instead, upon retirement a participant is entitled solely to whatever benefits can be provided by the amount credited to his or her individual account and the monies in one participant's account cannot generally be used to provide benefits to other participants. Thus, benefits would always be fully funded in such plans.

The insurance program was designed to be a self-supporting system financed by premiums levied on covered plans, assets of terminated plans, and employer liability assessments on employers of terminated plans. Non-multiemployer plans (generally, single employer plans and non-negotiated plans covering two or more employers) were fully covered immediately upon passage of ERISA. However, mandatory guarantees for multiemployer plans were deferred to January 1, 1978, with PBGC given discretionary guarantee authority until that date. 1/ On September 29, 1977, PBGC submitted a study to the Congress indicating that the current multiemployer premium rate ($.50 per participant) may have to be increased drastically to support the current insurance program when mandatory guarantees become effective for multiemployer plans. 2/ Moreover, this study pointed out the extreme uncertainty about the future incidence of multiemployer plan terminations and the potential adverse impact of the current termination insurance program on plan creations, growth of existing plans, and plan improvement. In response to these problems, Congress passed the aforementioned P.L. 95-214, which extended the discretionary program for multiemployer plan terminations until July 1, 1979 and directed PBGC to study further the problems of mandatory termination insurance coverage of multiemployer plans and to report its findings and possible solutions to the Congress by July 1, 1978. The July 1 report found that the cost of the current program could be much higher than was affordable and that the structure of the program was a major contributing factor to the potentially high cost.

NATURE AND HISTORY OF MULTIEMPLOYER PLANS

Multiemployer pension plans, as the term is used herein, are plans that cover the employees of two or more unaffiliated businesses and are maintained under one or more collective bargaining agreements. 3/

1/ The multiemployer plan termination program is financed solely by premiums paid by multiemployer plans, while the non-multiemployer plan program is financed solely by premiums paid by non-multiemployer plans.

2/ Potential Multiemployer Plan Liabilities under Title IV of ERISA, PBGC, September 29, 1977.

3/ It should be noted that this definition differs from the current statutory definition, see ERISA §3(37), which is proposed to be amended for certain purposes under ERISA. See discussion at p.17 below.

These plans have played a significant role in the growth of private defined benefit pension plan coverage over the past three decades. In 1950, multiemployer plans covered about one million participants, or about one-tenth of the 10 million participants in all private pension plans. 1/ Currently, about 8 million (one-fourth) of the approximately 33 million participants in all private defined benefit pension plans are covered by multiemployer plans. Thus, multiemployer plans have accounted for a substantial proportion of the increase in private pension plan coverage over the past three decades.

There are currently about 2,000 plans filing with PBGC as multiemployer plans. While multiemployer plans represent a small fraction of all plans covered by Title IV of ERISA (less than 3 percent), because of their size (an average of 4,000 participants as compared to an average of 300 participants for non-multiemployer plans), even a few terminations of such plans during a year would have a significant impact on the insurance program. 2/

Multiemployer plans tend to be concentrated in industries characterized by irregular employment, or by small employers, such as construction, water and motor vehicle transportation, trade, services, apparel industries, and printing and publishing. 3/ In these industries it would be impractical or uneconomical to establish single employer plans because

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1/ Multiemployer Pension Plans under Collective Bargaining, Spring 1960, Bureau of Labor Statistics, p.1; "Employee-Benefit Plans, 1975," Social Security Bulletin, November 1977, p. 27.

2/ The impact on the insurance program of even a few terminations of medium sized multiemployer plans is aptly illustrated by the experience with the Millinery Workers Retirement Fund and the Milk Industry Local 680 Pension Plan, which were granted discretionary coverage by PBGC. The Millinery plan had 4,300 participants with guaranteed benefits, while the Milk plan had 2,300. These plans represented a combined net claim of nearly $22 million on the insurance system.

3/ For example, about one-half of all covered multiemployer plans and about one-fourth of all participants are in the construction industry, which is characterized by irregular employment. These multiemployer construction industry plans cover about two-thirds of total construction industry employment. In water transportation, another industry characterized by irregular employment, nearly all employees in the industry -- about 200,000 -- are covered by multiemployer plans.

few workers ever remain long enough with one employer to qualify for a pension and/or because of the high attrition rate of small, and oftentimes, financially unstable, employers. 1/

Multiemployer plans have certain special characteristics that must be taken into account in designing a termination insurance program. Such plans typically provide portability of pension credit among contributing employers, so that participants do not lose pension credit if they shift among contributing employers. Moreover, multiemployer plans have provided a form of termination insurance, protecting participants against loss of benefits because of employers going out of business or otherwise abandoning the plan. The plans have typically provided that, once vested, a participant will not lose benefits even if his employer were to cease pension contributions. This latter feature, which provides valuable pension security to participants in multiemployer plans, makes such plans very susceptible to industry economic downturns or employer withdrawals. In such situations, the cost of funding unfunded vested benefits must be borne by a shrinking number of employers and their employees. As plan costs increase due to declines, further withdrawals may be precipitated, thus impairing the ability of the plan to continue. 2/

Another special feature of multiemployer plans is the manner in which contributions and benefits are determined. With few exceptions, contributions to the plan are specified in collective bargaining agreements, usually as a rate per unit of employment or production. Benefits are typically set by a joint board of trustees, based on an actuary's estimate of the benefit level that can be provided by the fixed contribution rate. This arrangement of providing defined benefits and fixed contributions and separating the cost and benefit determination processes is claimed by many plan sponsors to be essential to multiemployer plans. The fixed contribution aspect provides employers with known pension costs during the term of a bargaining agreement. This is important in industries like construction, where employers rely on set labor costs in bidding on projects. The separation of the cost and benefit determination processes is particularly useful where the plan covers a number of different bargaining agreements.

1/ See, for example, Multiemployer Plans under Collective Bargaining, Spring 1960, op. cit.; and Joseph J. Melone, Collectively Bargained Multi-Employer Pension Plans (Homewood, Illinois: Richard D. Irwin, Inc., 1963), pp. 7-8.

2/ In single employer situations, the deterrent in the current statute to plan abandonment by an employer is termination liability. Except for substantial employers (*basically*, ten percent contributors), there is no corresponding deterrent to individual employers abandoning a multiemployer plan.

IMPACT OF CURRENT TERMINATION INSURANCE PROGRAM ON MULTIEMPLOYER PLANS AND PARTICIPANTS

The two major objectives of termination insurance under ERISA are to protect plan participants against loss of benefits because of plan termination and to encourage the continuation and maintenance of private pension plans. The current multiemployer termination insurance provisions, if they become mandatory, are unlikely to accomplish either objective. The level of guarantees provided by the current program, which protect virtually all vested benefits, and limited employer liability make plan termination economically attractive when ongoing plan costs are high relative to plan benefits, as would be the case in declining industries. The ability of plans to transfer costs to the insurance program, at little or no risk to participants, poses extremely uncertain, but potentially very high costs for the insurance system. High premium costs could in turn make remaining plans less attractive, resulting in still more terminations.

The impact of the current insurance program is potentially greatest on plans in declining industries. As a plan's contribution base declines, it becomes necessary to increase contributions to support the benefits of former employees. Continued declines -- caused by attrition in employment, business failures, or voluntary withdrawals -- can result in continued increases in pension costs. At some point, the cost of continuing the plan (which represents wages deferred by active workers) may become much higher than the benefits that active employees will ever receive from the plan. ERISA generally, and Title IV in particular, present plans with the dilemma of either continuing at a high cost or terminating and transferring that cost to the premium system. Before ERISA, when few multiemployer plans terminated, the parties to plans went to great lengths to continue because of the economic cost of termination for plan participants. If the parties were unable or unwilling to increase contributions to maintain benefit levels, benefits were reduced to the level that could be supported by the existing contribution rate. However, ERISA limits the flexibility that plans previously had to deal with financial problems and eliminates much of the economic cost of termination without providing adequate deterrents to termination. Employer liability for unfunded guaranteed benefits, which is limited to 30 percent of net worth, is intended to deter avoidable

terminations. However, in industries with little or no net worth, which predominate in the multiemployer area, and in declining industries, employer liability may be much less than the cost of continuing the plan and terminations in such situations would result in large claims on the insurance system. The Milk and Millinery cases 1/ well illustrate the impact of the current employer liability provisions on plan costs and the insurance system in declining industry situations. In those cases, the guarantee protected virtually all vested benefits, but employer liability covered only about 20 percent of the unfunded guaranteed benefits.

Current provisions for employer liability on plan termination may also further increase the costs of the multiemployer termination insurance program. An unknown contingent liability payable on termination of a plan makes entry unattractive and creates incentives for employers to resist strongly improvement of multiemployer plans, thereby discouraging new entrants. It also encourages strong employers to withdraw at the first sign of plan decline in order to avoid being part of a "last man's club." Such withdrawals could precipitate plan failures.

The net result of the current termination insurance program could well be lower plan benefits, a reduction in the coverage of employees by defined benefit pension plans, and increasingly high assessments to pay for the cost of protecting employees against loss of benefits due to an event -- plan termination -- that is within the control of the parties to the collective bargaining agreement. Instead of raising the prospect of an immediate payment of up to 30 percent of an employer's net worth if a plan fails, it would be desirable that the financial obligation of employers that remain in a plan be limited to their required contribution rate.

Because of the inherent instability of the current program, its consequent risk of slowing the growth of multiemployer plans, and the potential costs of termination insurance, the current program must be revised to place primary emphasis on plan continuation.

1/ See footnote 2, p. 3.

The recommendations, which are discussed in the following section, would substantially reduce the impediments to multiemployer plan growth and continuance that ERISA presents. We believe that they will provide substantial protection of benefits in financially distressed multiemployer plans at reasonable cost to the multiemployer plan premium payers.

In the development of the recommendations, it was necessary to gain a thorough understanding of multiemployer plans, and to establish overall objectives for a termination insurance program that would be compatible with the operation of plans, and the economic and social milieu in which such plans operate. Accordingly, PBGC held continuing discussions with individuals and groups from all facets of the multiemployer pension community, as well as the PBGC's Advisory Committee, in an effort to develop a program that reflects a thorough understanding of the nature of multiemployer plans, the environment in which they operate, and the likely impact of ERISA and possible legislative changes on those plans, the parties to them, and the insurance program. Four objectives for a multiemployer termination insurance program emerged from these discussions:

1. The program must be compatible with the collective bargaining process.

2. The program should limit the liability of employers to their required contribution rate.

3. The program must prevent avoidable cost transfers to the insurance system while providing protection to employees in dying industries.

4. The program must protect responsible plans from having to assume the cost of plans providing overly generous benefits.

The recommendations were designed to meet all of these objectives, with major emphasis on compatibility with the collective bargaining process. It is this process that establishes and maintains multiemployer plans and, in the final analysis, assures plan continuation.

RECOMMENDATIONS

The recommendations for restructuring the multiemployer termination insurance program, which are discussed in greater detail below, are:

1. A program of plan reorganization for plans in a financially precarious position. This program provides relief from escalating contribution requirements, and contains restrictions on excessive benefit increases, in order to avoid the need to terminate because of the financial burden of continuing to fund the plan.

2. Revise the guarantee program to make plan "insolvency" the only insurable event with guarantees provided in the form of direct financial assistance (loans) to "insolvent" plans. The basic level of guarantees would be lower than the current program, but with a floor guarantee of $100 per month and a maximum guaranteeable benefit of $500 per month.

3. A revision of the termination rules to require that contributions to the plan continue despite termination. The plan would continue as a separate legal entity and PBGC would not pay any monies until plan insolvency (i.e., plan assets plus employer contributions become insufficient to pay guaranteed benefits). Termination would end vesting and accruals but not the funding obligation.

4. Revisions in the minimum funding standards designed to assure that contributions to a multiemployer plan will be sufficient to pay benefits except in the case of a severe decline in the plan's contribution base.

5. A requirement that an employer that withdraws from a multiemployer plan finish funding a reasonable share of unfunded benefit liabilities.

6. Revision of the definition of multiemployer plan for certain purposes to eliminate the uncertainties and administrative problems that arise under the current definition.

7. Revision of the merger and transfer rules to ease the administrative burdens associated with a merger.

8. Revision of the premium structure and premium level for multiemployer plans.

1. Plan Reorganization

The cost of the termination insurance program under ERISA is highly uncertain and potentially very large because ERISA does not offer plans adequate alternatives to termination in terms of benefit protection and control of costs. When a plan's contribution base declines, the cost of maintaining the plan escalates for remaining employers and employees. Before ERISA, the parties to a multiemployer plan could control excessive cost increases by reducing benefits. Benefit reductions enabled plans to continue in the face of contribution base declines, thereby enabling participants to earn additional vesting and accruals and assuring that plan funding would continue. ERISA virtually eliminated this flexibility while allowing shifts of plan liabilities to PBGC premium payers -- the other multiemployer plans -- through termination. Thus, ERISA reduces or removes the incentive to continue a plan that has become expensive, and creates some disincentives to fund more rapidly than is required to meet minimum funding standards and pay benefits. Consequently, the termination insurance program will be faced with costs that would have been borne by the parties through continuation of the plan in the pre-ERISA period and that are likely to be more than the multiemployer plan premium payers can be expected to pay.

In order to encourage the continuation and maintenance of multiemployer plans, the PBGC recommends a program of plan reorganization that provides the parties to collective bargaining adequate flexibility to restore a financially unsound plan to a sound condition. 1/ Plan reorganization is a program which requires the parties to plans identified as being in financial difficulty to take corrective action to improve the balance between promised benefits and contributions, and provides severely distressed plans relief from escalating costs because of contribution base declines. Plan reorganization works within the framework of the collective bargaining process by giving the parties various options to shape their reorganization remedies and by insulating employers that stay in the plan from any liability under the insurance program beyond the negotiated contribution rate, regardless of what happens to the plan.

Under the recommended reorganization program, the parties would be required to take steps to restore a sound financial condition to the plan. The options available to the parties to accomplish this end are: increases in contributions,

1/ The determination of financial condition will be based on a comparison of the plan's unfunded liabilities with its contributions.

reductions in benefits to a specified level (but not below the guaranteed level), or both. Funding waivers would be available to protect plans against escalating funding costs because of declines in their contribution base. If the plan becomes unable to pay benefits, the insurance program would provide needed funds in the form of loans sufficient to allow payment of guaranteed benefits. Thus, plan reorganization would allow sponsors of plans in financial difficulty to protect themselves against ever-escalating contribution rate requirements without terminating the plan.

The reorganization rules would be implemented in a manner that would not require plans that are already heavily burdened with costs to automatically increase contributions or reduce benefits.

Plan reorganization, which provides an objective basis for providing support through the insurance program to those plans that have taken self-corrective action and nevertheless would have no recourse but to terminate in the absence of such support, is in effect "no-fault" insurance. A plan that requires PBGC assistance payments in reorganization is in this position generally because of events outside the control of the plan (*i.e.*, industry declines). 1/ There is little incentive to maneuver a plan into reorganization because reorganization requires sacrifices by one or both of the parties, in the form of higher contributions or reduced benefits; assistance would only be payable to plans that experience continued declines while in reorganization; and assistance would be a loan that must be repaid if the financial condition of the plan improves (this could happen if the decline in employment either ends or, in fact, is reversed). Consequently, the recommended program substantially reduces or removes the potential for avoidable cost transfers to the insurance system, thus eliminating many, if not most, of the uncertainties that arise under the current program where the insured event -- termination -- is within the control of the parties.

1/ On a prospective basis, only plans that suffer declines in the contribution base would be eligible for assistance because of the manner in which the proposed reorganization program and recommendations for revising minimum funding standards, which are discussed below, operate. Because of the lack of sound funding standards in the pre-ERISA period, it is possible that some plans may be currently, or shortly, in need of assistance for reasons other than a decline in the contribution base. However, on the basis of PBGC's analysis of the current financial status of multiemployer plans, this appears to be an unlikely possibility.

Financial assistance to reorganized plans provides substantial incentives for plan continuation, which in the final analysis, may provide participants with maximum benefit security. Reorganization assistance can also be expected to be least disruptive on the collective bargaining process and the framework within which multiemployer plans were established and operate. In addition, it avoids the tremendous administrative burden on plans and the PBGC that termination of a multiemployer plan would involve, i.e., benefit and guarantee determinations for a large number of participants and employer liability determinations for a large number of employers.

2. Guarantees

The PBGC recommends a lower guarantee for multiemployer plans than under the current statute. A lower guarantee is necessary for the following reasons:

(1) Claims are uncertain even under a "reorganization assistance only" program.

(2) The guarantee level should be supportable by a premium similar to the single employer rate.

(3) A lower guarantee creates a stronger disincentive to let a plan fall into reorganization.

The recommended basic guarantee for multiemployer plans under the proposed program is 60 percent of the current statutory guarantees (with a modified phase-in rule) and a floor of $100 per month and a maximum guaranteeable benefit of $500 per month. The guarantee of benefit increases would be phased-in over five years, beginning after a three-year delay. 1/ The $100 minimum guarantee provides protection to participants in low benefit plans, and to retirees. The $500 maximum guaranteeable benefit assures that low benefit plans are not required to subsidize high benefit plans, especially where benefit promises may have resulted from overly optimistic assumptions about the plan's contribution base or investment return.

1/ Benefit increases made when a plan has a shortfall would not be guaranteed if the plan enters reorganization in three years. Also, benefit increases made in reorganization would not be guaranteed.

In order to provide higher levels of protection to participants in plans with a sound balance between contributions and benefits, without exposing the insurance system to unreasonable risks, PBGC believes a program of guarantees above the basic guarantee ("a second tier of guarantees") should be available to plans that meet certain criteria but nevertheless become insolvent because of severe or protracted declines in their contribution base. Such criteria could focus on, for example, the ratio of plan assets to guaranteed benefits, and the funding rate for amortizing unfunded guaranteed benefits.

It is recommended that the PBGC be required to review the guarantee structure within five years and to recommend any justifiable changes. If at any time the premium revenue becomes inadequate to support the guarantee, the PBGC would be required to request from the Congress a premium increase. If the increase is not granted, the guarantee would be adjusted accordingly.

3. Termination: Freezing of Accruals and Vesting

The purposes of the proposed plan reorganization program are to protect participants against benefit losses and to prevent avoidable cost transfers to the insurance system. However, as long as plans can terminate, participants may be subject to benefit losses. In order to assure that benefits are not sacrificed by termination of a plan, it is recommended that the statute be revised to prohibit the parties from completely abandoning a multiemployer plan. Instead, the parties would be permitted to terminate the plan by freezing benefit accruals and vesting. Employers would be obligated to continue to fund the frozen plan. 1/ Reorganization would be available to the plan if it should encounter financial difficulty, despite the freeze, because of industry declines. Also, plans already in reorganization would be permitted to freeze.

Employers in a frozen plan would have the option of staying in the plan or withdrawing and paying withdrawal liability, just as they would in an ongoing plan. If all employers withdraw, a trustee would be appointed to administer the plan -- i.e., collect withdrawal liability and pay benefits. Benefits would be reduced if withdrawal liability payments are not sufficient to pay the benefits, but benefits could not be reduced below the guaranteed level just as in an ongoing plan.

1/ The parties would not be permitted to reduce *contributions* because of the freeze. This would discourage unnecessary freezes. Also, consideration needs to be given to limitations on new or existing supplemental plans to prevent freezes which may discriminate against one group of participants.

The effect of the PBGC recommendations for reorganization and freezing is that premium funds would be used to pay benefits in a multiemployer plan only when the plan becomes unable to pay the guaranteed level of benefits from plan assets and contributions. This would make plan insolvency the sole insurable event. The net cost to the insurance system for a plan would be the amount of assistance payments that exceed the amount of future contributions to the plan.

4. Minimum Funding Standards

The minimum funding standards for multiemployer plans under ERISA do not assure that a plan will have enough funds to pay promised benefits when they become due. ERISA permits plans to defer funding of liabilities far into the future. For example, ERISA permits 40-year amortization of unfunded past service liabilities created by retroactive benefit increases, and 20-year funding of experience losses as well as shortfalls under the shortfall funding method. As a result of this deferral of costs, a plan can be faced with the need to greatly increase its contribution rate in order to amortize its accumulated unfunded liabilities (fixed costs) and pay retirees' benefits even in the absence of a decline in the plan's contribution base. This effect is exacerbated if the plan's contribution base declines so that fixed costs must be spread over a smaller number of active employees.

To alleviate this problem in the future, it is recommended that minimum funding standards be revised to:

(1) Reduce the amortization period for funding past service liabilities created by future amendments increasing benefits from 40 to 30 years, and reduce the amortization period for funding experience losses from 20 to 15 years. 1/

(2) Reduce the period allowed for funding future shortfalls in contributions that occur when a plan's actual contribution base is less than the estimated contribution base, to 15 years from the year in which the shortfall occurred. Plans would be permitted to delay commencement of the funding of a shortfall for up to 5 years.

1/ This proposal eliminates the differential that ERISA established between multiemployer and single employer plans. This change is believed necessary to assure adequate funding of multiemployer plans.

(3) Require plans to fund at least a minimum percent of the unfunded vested liabilities in each year. The PBGC recommends a minimum contribution equal to approximately 10 percent of the plan's unfunded vested liabilities. 1/

These new rules would be designed in a manner that would not create excessive increases for plans that are or may become heavily burdened with costs. The minimum funding standards would be counterproductive if they impose additional funding requirements that plan sponsors are unwilling to bear.

The recommendations have a three-fold purpose:

(1) To prevent financial problems from developing in healthy plans, without unduly increasing costs in those plans.

(2) To assure that financially weakened plans have sufficient assets to make current benefit payments.

(3) To relieve plan sponsors of excessive cost increases due to severe contribution base declines.

Funding standards require plan sponsors to begin funding promised benefits as soon as the benefits are earned. Thus, a plan will build up an asset reserve to cover at least a portion of the cost of those benefits before the plan must pay the benefits to participants. The portion of benefit payments that is not funded in advance must be paid from current contributions.

Sound funding standards will require that contributions be set at a level that will assure that plans have sufficient funds to pay benefits when due without having to greatly increase contributions in the future.

The recommendations for faster funding of future benefit increases and shortfalls are designed to do this for most plans. A plan that has a stable or growing contribution base generally should have sufficient funds to pay benefits when they fall due, if the plan funds benefit increases over 30 years and funds future shortfalls over 15 years, with funding of a shortfall beginning no later than 5 years after the shortfall occurs.

1/ Ten percent is based on an assumed interest rate of five percent. The ten percent figure would be adjusted to conform to the interest rate assumption an individual plan uses to value its liabilities and determine its required contribution rate.

These revised standards, however, will not avert cash flow problems in a plan that has accumulated large unfunded liabilities relative to contributions as a result of past benefit setting practices, past funding practices, contribution base declines or poor investment experience.

For these plans, higher contributions than those that would be required by 40-year funding of future benefit increases and 15-year funding of shortfalls are needed. Accordingly, PBGC recommends that plans be required to contribute an annual amount of no less than 10 percent of unfunded vested liabilities in the plan. The 10 percent rate would generally assure -- absent a severe decline in the plan's contribution base -- that the plan has sufficient funds to pay retirees' benefits and would help assure that the benefits of active participants are better funded at their retirement. 1/

5. Withdrawal of an Employer

Cessation of contributions by a contributing employer to a multiemployer plan can be harmful to the plan, the remaining employers, and the insurance program. When an employer withdraws, remaining employers have an increased funding burden since they must now pay the past service costs previously carried by the withdrawn employer. If the decline in the contribution base continues, plan costs will escalate, making the plan less and less attractive to both new entrants and current employers and employees. Eventually, a plan could find itself so overloaded with unfunded past service costs that reorganization is necessary (or termination would be attractive to active employees, even in the absence of guarantees).

The PBGC recommends requiring an employer that leaves a plan to compensate the plan for the loss to the plan's contribution base, to avoid shifting costs from the withdrawing employer to the remaining employers. The recommended rules would require such compensation for a complete and permanent cessation of contributions by an employer, or for a substantial partial and permanent cessation in that employer's

1/ Generally, a plan that is paying out ten percent or more of its unfunded vested liabilities in benefits each year is a plan which has an extremely high proportion of its total liabilities attributable to retirees.

contributions to the plan. 1/ Because the intent of the rules is to indemnify a plan primarily for withdrawals that cause a net reduction in the plan's contribution base, the rules would not require a plan to seek compensation for withdrawals by small employers or partial withdrawals by large employers that do not significantly reduce the plan's contribution base, *e.g.*, relocations within the geographical area covered by the plan. 2/

Requiring withdrawing employers to compensate the plan would create a financial disincentive to withdraw and would protect remaining employers against increased costs for voluntary withdrawals that do occur, *i.e.*, withdrawals that result from employer and employee decisions. Withdrawal liability for unfunded vested liabilities would also help assure that the costs transferred to other multiemployer plans through payment of guaranteed benefits by the PBGC are the costs of industry decline and not costs of voluntary abandonment of a plan by an employer or group of employees.

The current ERISA withdrawal rules, which apply only to substantial employers, allocate liability to withdrawn employers based on their proportionate share of total plan contributions during the five years preceding their withdrawal. While this allocation rule has administrative advantages for plans, it may not be the most equitable or desirable method for allocating unfunded vested liability for all plans. For example, this method may impose restraints on plan entry, since new employers would be liable for any unfunded liability created before their entry. Therefore, PBGC recommends that a plan be given the flexibility to adopt, from various alternatives, the allocation method that is best suited to its own circumstances.

Included among the alternatives would be the current method for allocating unfunded liability, and a method that would allocate the existing unfunded vested liability to all employers participating in the plan as of a date specified

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1/ Special rules would apply to the construction industry to assure that a withdrawing employer is required to pay a plan only when the employer continues to work in the plan's jurisdiction. For example, an employer who works only temporarily in the jurisdiction of a plan would not be subject to withdrawal liability upon leaving that jurisdiction.

2/ The rules might have specified a net reduction in the plan's contribution base (instead of a facility closing) as the "event" that creates liability. However, identifying such situations would be difficult and might result in employers having to pay a plan for temporary reductions in the plan's contribution base.

in the statute, with new employers being liable only for unfunded vested liabilities created during their period of participation in the plan in proportion to their contributions.

6. Definition of Multiemployer Plan

A revised definition of multiemployer plan for insurance and certain other purposes under ERISA that would treat as one class of plans all collectively bargained plans to which two or more employers contribute is recommended. This class of plans was divided into two classes by ERISA, which considers a plan a multiemployer plan (1) only in a plan year in which no employer makes more than a specified percentage of the contributions for that year, and (2) only if the plan provides benefits to plan participants, even if their employer ceases contributions to the plan, except that the plan may disregard benefits accrued as a result of service with the employer before the employer's entry into the plan. These revisions are necessary to eliminate problems for both PBGC and plans in determining the status of a plan, since, for example, a plan's status could be affected by events outside its control, such as declines in contributions by some employers accompanied by increases for a large employer. The revisions are also necessary to prevent plans from moving in or out of the multiemployer program merely by virtue of a plan amendment.

The benefit preservation rule with its permissible reductions for prior service, which is an exception to the ERISA vesting rules, should be transferred to the vesting sections of the Act. Thus, plans which are multiemployer plans for Title IV purposes would continue to be allowed to disregard the benefits of participants of a withdrawn employer attributable to service with that employer prior to its entry into the plan.

7. Mergers and Transfers

ERISA does not provide specific statutory rules for mergers and transfers involving multiemployer plans. Instead, it gives the PBGC authority to apply to multiemployer plans the rules for non-multiemployer plans to the extent PBGC determines appropriate. ERISA contains a test to assure that funded benefits are not diluted by a merger or transfer of assets and liabilities. If this test were to be applied to multiemployer plans, PBGC believes that it would, as a practical matter, prevent mergers and transfers of multiemployer plans because of the administrative burdens it would impose on plans.

It is recommended that mergers and transfers be permitted subject to a plan continuation test and a business purpose test. The plan continuation test would apply the reorganization threshold tests to identify a merger or transfer which would put a plan in danger of failing.

8. Program Financing

The cost of the recommended guarantee program is uncertain, because it will depend on such factors as future general and industry economic conditions. However, the current premium of 50 cents per participant is below the lowest estimated cost for financing the recommended program. Estimates of the cost of the recommended program, exclusive of administrative costs, range from 75 cents to $3.70. The 75 cent rate is the estimated cost of providing assistance, as long as necessary, to plans that first require assistance during the first 10 years of the program. The $3.70 rate is the cost of providing such assistance to all plans that would first require assistance over the first 20 years of the program. The minimum estimate is clearly insufficient to soundly finance the insurance program, since it completely ignores claims that are likely to occur in the second 10 years of the program. The maximum estimate appears to be higher than what the actual cost of the program will be, since it is based on plans experiencing sustained rates of decline over a period of up to 20 years. Thus, the premium rate necessary to finance the recommended program lies somewhere between these two extremes -- substantially higher than 75 cents, but somewhat lower than $3.70. PBGC, therefore, recommends a premium averaging $2.60 per participant, which is the same rate paid by non-multiemployer plans.

The premium charged to individual plans should reflect the risk and exposure of a plan. Such a structure, however, may impose high administrative costs on both plans and PBGC. Therefore, it may be necessary to assess the premium on a per participant basis initially. Thus, it is recommended that PBGC be authorized to develop alternate premium structures, including one reflecting individual risk and exposure, and a uniform premium rate, as is currently in effect. PBGC would be required to review premiums at least every five years in terms of their adequacy to support anticipated claims. If a premium increase is necessary to support the existing guaranteed level, but is not granted by the Congress, the guarantee would be adjusted accordingly. Conversely, if premiums are higher than necessary, PBGC would be authorized to increase the guaranteed level.