



WASHINGTON *Update*

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Congress Passes Pension Protection Act That Includes Significant Multiemployer Plan Changes

On August 3, 2006, the U.S. Senate approved the long-awaited pension reform bill, the Pension Protection Act of 2006 (the PPA), by a vote of 93-5. The PPA was passed a week before by the U.S. House of Representatives and was approved by the Senate without amendment. The president signed the PPA into law on August 16. The PPA makes important and far-reaching changes to the federal laws governing traditional single employer defined benefit plans, multiemployer pension plans, “cash balance” and pension equity plans, 401(k) and other types of defined contribution plans and individual retirement accounts. The focus of this “Washington Update” is on some of the major changes for multiemployer plans.

The PPA preserves the funding standard account approach under current law. However, new plan liabilities due to benefit increases and changes in actuarial assumptions will have to be amortized over 15 years instead of 30, and short-term benefits will need to be funded by the time they are fully paid out. Plans will not have to recalculate amortization schedules already in effect. While the current minimum funding approach will remain, there are new options to avoid funding deficiencies (and to defer or avoid the excise taxes that would otherwise be imposed). Multiemployer plans facing a funding deficiency within ten years can extend the amortization period for funding liabilities for up to five years with minimal IRS review. To qualify, a plan’s trustees must adopt a program to correct the plan’s funding problems, certify that

the extension will resolve the funding problem and provide notice of the extension to all affected parties (IRS has the discretion to grant an additional five-year extension).

The PPA also creates two new categories for troubled multiemployer plans, “endangered status” plans and “critical status” plans. New funding requirements and other rules on each category are provided by the PPA. Generally, a plan’s status is based on funding percentages and projected accumulated funding deficiencies. A plan that is more than 64% but less than 80% funded, or has an accumulated funding deficiency in the current year or in any of the next six years, is in “endangered status” (and if the plan meets both criteria, it is in “seriously endangered” status). A plan is in “critical status” if (1) it is less than 65% funded, and assets plus contributions are insufficient to make benefit payments for the current year and the next six years; (2) it will experience a funding deficiency in the current year or in the next three years (four years if less than 65% funded); (3) its normal cost plus interest exceeds contributions, the present value of benefits for inactive participants is higher than the present value of benefits for active participants, and a funding deficiency is projected within five years; or (4) its assets plus five years of contributions are less than five years of benefits plus administrative expenses.

Within 90 days after the start of the plan year, a multiemployer plan’s actuary must certify whether the plan is in endangered or critical status for the plan year. Failure to do so is treated as a failure to file the annual report (and a penalty of up to \$1,100

per day applies). If a plan is certified to be in endangered or critical status, the plan's trustees must notify the plan's participants and beneficiaries, bargaining parties, the Pension Benefit Guaranty Corporation and the Department of Labor within 30 days after the date of certification.

The trustees of a plan in endangered status must adopt a funding improvement plan (FIP) within 240 days of the deadline for certifying the plan's status. If the trustees fail to adopt an FIP by the end of the 240-day period, a penalty of up to \$1,100 a day applies. An FIP is a plan consisting of options to be proposed to the bargaining parties that are designed to bring the plan's funding up to certain benchmark levels by the end of the funding improvement period (a ten-year period that begins after the earlier of (1) the second anniversary of the adoption of the FIP or (2) the expiration of collective bargaining agreements that were in effect when the actuarial certification was due, and that cover at least 75% of the plan's active participants at that time). For plans that are not in seriously endangered status, the FIP must aim to reduce the percentage of underfunding by one-third by the end of the funding improvement period. Plans in seriously endangered status must try to reduce the percentage of underfunding by one-fifth in 15 years.

The trustees of a plan in critical status must adopt a "rehabilitation plan" within 240 days of the date actuarial certification was required; failure to do so can result in a penalty of up to \$1,100 a day. A *rehabilitation plan* is a plan consisting of options to be proposed to the bargaining parties that are designed to have the plan emerge from critical status by the end of the rehabilitation period (generally, the same as for a funding improvement period as noted above). If the trustees determine that it is not reasonable to expect that the plan will emerge from critical status by the end of the rehabilitation period, the plan must include measures to emerge from critical status at a later time or to forestall possible insolvency. The rehabilitation plan may include reductions in plan expenditures, reductions in future benefit accruals or increases in contributions, if agreed to by the bargaining parties, or any combination of such actions. A rehabilitation plan must provide annual standards for meeting the requirements of the rehabilitation. The trustees must update the plan annually and file the update with the plan's annual report.

Additionally, the PPA provides that, despite the anticutback rules, the trustees of a plan in critical status may reduce "adjustable benefits" if they deem reductions to be appropriate, subject to the outcome of bargaining over the schedules provided by the trustees. "Adjustable benefits" include (1) benefits and features, including postretire-

ment death benefits, disability benefits not in pay status and similar benefits; (2) any early retirement benefit or retirement-type subsidy and any benefit payment option (other than the qualified joint and survivor annuity); and (3) benefit increases adopted or effective fewer than 60 months before the plan entered critical status. The trustees may not reduce adjustable benefits in pay status before notifying participants, beneficiaries, employers and unions that the plan is in critical status and that adjustable benefits may be reduced. Notice of any reduction of adjustable benefits must be provided at least 30 days before the reduction is effective. Furthermore, trustees also may not reduce a participant's accrued benefit payable at normal retirement age, except for increases that had been adopted fewer than 60 months before the plan entered critical status.

The PPA also provides that if an FIP or a rehabilitation plan requires an employer to make contributions to the plan, an excise tax applies upon the failure to do so. The amount of the tax is equal to the amount of the required contribution the employer fails to make.

The new system suspends the excise tax that currently applies to plans with accumulated funding deficiencies for plans in critical status. Employers can escape the excise tax while a plan is in critical status as long as they are implementing a program to improve the plan's funding status. However, once employers are notified that a plan is in critical status, an additional required contribution (surcharge) is imposed. In the first plan year of critical status, the surcharge equals 5% of the contributions an employer is required to make. The surcharge increases to 10% of required contributions in succeeding plan years if the plan remains in critical status. Failure to make the surcharge payment is treated as a delinquent contribution. The surcharge is no longer required when a collective bargaining agreement includes terms consistent with a schedule under a rehabilitation plan that a plan's trustees are required to adopt. Contributions attributable to the surcharge may not be the basis for any benefit accrual.

Finally, the PPA raises the limit on deductions for employer contributions from 100% to 140% of current liability and eliminates the combined defined contribution/defined benefit plan deduction limit that currently restricts employer contributions to a defined contribution plan.

It is important to note that these are just some of the major provisions in the PPA, and plan sponsors and contributing employers are encouraged to carefully review the law.

The full text of the PPA can be found at frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=109_cong_bills&docid=f:h4enr.txt.pdf. 