

Pension Protection Act of 2006 Overview of Multiemployer Pension Plan Provisions

*courtesy of the Sheet Metal and Air Conditioning Contractors' National Association
(SMACNA)*

On August 17, 2006 President Bush signed The Pension Protection Act of 2006 (PPA), PL 109 - 280, which the Senate and House passed before leaving for summer recess. The new law applies to all single employer and multiemployer defined benefit pension plans, including the National Pension Fund and local multiemployer pension funds. The new law preserves important differences in funding rules for single employer plans and multiemployer plans. This was a critical issue for union contractor associations which actively lobbied on the issue with the Multiemployer Pension Plan Coalition, a broad-based, multi-industry, labor-management coalition.

Most of the law's provisions are effective in 2008 and plan professionals are in the process of educating themselves about the provisions and how they will affect plan funding, planning and investing. Regulations will be written to further clarify how the law will be implemented. Although certification is not required until after the 2007 plan year and even though some factors that will determine plan status in 2008 can't be ascertained in advance, plan actuaries will be analyzing how the law will affect their plan's funding status.

The law makes some welcome general changes in funding rules but will also impose discipline on plans with funding problems and require those plans to take action to improve their funding status. Once the law goes into effect, fund actuaries will have 90 days after the start of the plan year to certify the status of the plan for that year and to project the funding standard account for the ensuing six years.

If a plan has funding problems, trustees then have 30 days after the actuarial certification to notify the stakeholders and approximately eight months after the certification to develop schedules to present to the bargaining parties. The schedules must be designed to meet the statutory funding requirements before the funding improvement period end. For multiemployer plans in the worst shape, the law also makes changes in the anti-cutback rules to give plans the option of making changes in some retirement benefit features, such as payment options, disability benefits, and early retirement benefits, for people who have not yet retired. The new law also outlines new disclosure rules for all plans with added disclosure requirements for financially troubled plans.

The law requires a study on the effect of the changes, including the effect of the law on the financial status of small employers, with a report due no later than December 31, 2011. The law's provisions for plans with serious funding problems sunset December 31, 2014. However, Funding Improvement and Rehabilitation Plans in effect at the time of the sunset continue.

A more detailed summary of the law by the Congressional Joint Committee on Taxation can be viewed at: <http://www.house.gov/jct/x-38-06.pdf>

GENERAL FUNDING RULE CHANGES

The new law will force faster funding of new obligations. The new law:

- will now require benefit changes and increases and changes in actuarial assumptions to be amortized over 15 years instead of 30 years (amounts being amortized under old amortization rules are not recalculated).
- requires short-term benefits such as 13th checks to be funded over the payout period.

The new law encourages plans to build a funding cushion. The law:

- raises the limit on deductions for employer contributions to 140% of the plan's current unfunded liability up from 100%, avoiding forced increases in benefits due to temporary gains in assets. (Effective 2006 tax year)
- eliminates the 25% of compensation combined limit on contributions for defined benefit and defined contribution plans. (Effective 2006 tax year)

The law gives ready access to IRS relief procedures. The law in prescribed circumstances:

- would require the IRS to permit plans facing a funding deficiency within 10 years to extend the amortization schedule for paying down its liabilities by 5 years, (with a 5-year extension possible)
- would require those plans to adopt some type of recovery plan and abide by some less favorable interest rule changes, and
- would require the IRS to permit plans to go on and off shortfall method every five years with no increase in benefits while the method is in use.

PLANS WITH FUNDING PROBLEMS MUST TAKE ACTION

Endangered Status Definition: A plan is in **Endangered Status** if (1) it is less than 80% funded OR (2) the plan is projected to have a funding deficiency within

7 years (and if the plan is not already in Critical Status). A plan less than 80% funded AND projected to have a funding deficiency within 7 years is considered **Seriously Endangered**. (Funded Percentage = Plan Assets/Accrued Liability)

Once in Endangered Status:

- Plans have roughly one year to develop and approve a “Funding Improvement Plan” designed to reduce the amount of under-funding.
- Endangered Plans have 10 years to improve funding. They must improve their funding percentage by one-third of the difference between 100% and the plan’s funded percentage from the **earlier** of two years after the adoption of the funding improvement plan **or** the plan year following the expiration of CBAs covering 75% of active participants. (For example: Plan 73% funded must improve to 82% funded over 10 years)
- Seriously Endangered Plans below 70% funded have 15 years to improve funding. They must improve their funding percentage by one-fifth of the difference between 100% and the plan’s funded percentage from the **earlier** of two years after the adoption of the funding improvement plan **or** the plan year following the expiration of CBAs covering 75% of active participants. (For example: Plan 60% funded must improve by 8% to 68% funded over 15 years.)
- Benefit improvements are restricted if not part of the Funding Improvement Plan.
- Plans have additional, specific notification requirements if they are in Endangered or Seriously Endangered Status.

If the bargaining parties fail to agree to a funding improvement plan, a default schedule applies. The default schedule would be reductions in future accruals to the maximum extent permitted by law assuming no contribution increases. Additional contributions would apply only if necessary to achieve the funding improvement required by the law.

Moving out of Endangered Status: A plan moves out of endangered status in any plan year in which the triggers are no longer tripped (or when the plan goes into critical status).

Critical Status

Definition: A plan is considered in Critical Status

- if it is less than 65% funded and with a projected funding deficiency within 5 years, or the inability to pay benefits within 7 years;

- if it has a projected funding deficiency within 4 years, or an inability to pay benefits within 5 years, regardless of its funded percentage; and
- if it has benefits for inactives that are greater than for actives, contributions that are less than carrying costs and a funding deficiency projected within 5 years.

Once in Critical Status:

- Plans have roughly one year to develop and approve a “Rehabilitation Plan” designed to reduce the amount of under-funding.
- Employers will not be required to make “lump sum” payments normally required to meet the minimum funding standard when a plan has an accumulated funding deficiency.
- Employers will not be subject to an IRS excise tax penalty if a funding deficiency does occur, as long as the parties fulfill their obligations under the Rehabilitation Plan and under the bargaining agreements negotiated to improve funding.
- Changes in the anti-cut back rules apply so that plans have the ability to reduce or eliminate early retirement subsidies and other adjustable benefits to help improve funding status
 - if agreed to by the bargaining parties,
 - except that core retirement benefits payable at normal retirement age cannot be changed, and
 - with the exception that plans may not cut back benefits of people who retired before being notified of the plan’s critical status.

Adjustable benefits include certain retirement benefit features, such as payment options, disability benefits, and early retirement benefits, reduction of joint and survivor annuity if above 50% and benefit increases adopted or effective fewer than 60 months before the plan entered critical status.

- Plans must notify all parties within 30 days after critical status determination is made.
- Thirty days after notification of critical status a 5% employer surcharge based on contribution rates applies to keep the fund from further deterioration while a rehabilitation plan is developed and approved. The surcharge moves to 10% the second year and stays in effect until the rehabilitation plan has been approved. During this interim period, neither benefit improvements nor any reduction in contribution levels are allowed.

The surcharge is not required beginning on the effective date of a CBA (or other agreement) that includes terms consistent with a schedule presented by the plan sponsor for the Rehabilitation Plan.

- Plans have 10 years to move out of critical status from the earlier of two years after adoption of the Rehab Plan or the first plan year after the beginning of CBAs covering 75% of active participants with extension available.

If the bargaining parties fail to agree to a funding improvement plan, a default schedule applies. The employer surcharge stays in effect but the default schedule assumes no increases in contributions except as necessary to emerge from critical status after benefit accruals and other benefits have been reduced to the maximum extent permitted by law.

Moving out of Critical Status:

A plan moves out of critical status when it no longer projects a funding deficiency within 10 years.

DISCLOSURE REQUIREMENTS

The law requires that more information be available in a timely manner for stakeholders.

- Annual funding notices must be sent out 120 days after the end of the plan year (instead of 11 ½ months after the end of the plan year) and include much more information.
- For plans in Endangered or Critical Status, the actuary must certify whether or not the plan is making scheduled progress. Annual reports must contain updates on Funding Improvement or Rehabilitation Plans.
- Notification of Endangered or Critical status must be provided to participants, beneficiaries, bargaining parties, the PBGC and the Secretary of Labor within 30 days after endangered or critical status is determined.
- The Labor Department will post information from plans' annual reports on the Internet and plans will be required to provide certain other materials to employers on request. Plans with funding problems face additional notice requirements.

WITHDRAWAL LIABILITY CHANGES

The new law makes some relatively minor changes in withdrawal liability rules. Very generally, the law provides:

- **Fresh Start and Free Look for Construction:** The new law updates old rules which sometimes encumbered employers with withdrawal liability even if the plan were fully funded. Under certain conditions, trustees can now adopt a “fresh start” rule for contractors when plans become fully funded. (Effective January 1, 2007)

Construction industry plans can adopt a “free look” rule. Under certain conditions, the rule allows a new contributing employer to avoid withdrawal liability if its contribution obligation lasts no longer than the number of years required for vesting.

- The law also updates the solvency tables for ERISA Section 4225 (a), extends partial withdrawal liability in the case of work transferred to an entity or entities owned or controlled by the employer, establishes new procedures applying to disputes involving withdrawal liability for small employers (those with no more than 500 employees and required to make contributions for no more than 250 employees).

TAX PROVISIONS

The new law enhances retirement tax breaks, adds charitable giving limits, including a change for S-corporation shareholders, and makes permanent the increases in section 415 limits adopted in 2001 and other tax changes.

If you have any comments or questions, please contact SMACNA’s Capitol Hill Office at 202.547.8202.

As always, SMACNA members and chapters are advised to consult with their attorneys and actuarial/accounting consultants with regard to changes in ERISA and tax laws.