
CRITICAL AND DECLINING STATUS
AND BENEFIT SUSPENSIONS

Prepared by:
BEYER-BARBER COMPANY



PART I

BACKGROUND



CRITICAL AND DECLINING STATUS DETERMINATION

- The determination as to whether a Fund is, or is not, in **Critical and Declining Status** is done in much the same way as is the determination of **Endangered** or **Critical** Status. They are based on:
 - forecast projections based on the prior year's Actuarial Valuation Report,
 - actuarial assumptions like interest rate and mortality tables for future years, and
 - projected work levels for future years.

- The main difference is that the forecast projections used for **Endangered** and **Critical** Status are based on 10 year projections using only the contribution increases that have already been negotiated while those used for the **Critical and Declining Status** are based on 20 to 30 year forecasts and future contribution increases required by the Rehabilitation Plan whether or they've been negotiated or not.

CRITICAL AND DECLINING STATUS DETERMINATION

- The criteria as to whether this Fund is in **Critical and Declining Status** is based on whether the Fund is projected to run out of money within 15 to 20 years.
- Until such time as this determination is made, we outline the steps a Fund would have to undertake to determine whether, and to what extent benefit suspensions would be prudent and the challenges that they present.
- The following is an extensive list of steps required. While regulations have already been issued, the IRS has reserved the right to make changes in the future.

PART II

STEPS AND CHALLENGES



STEPS AND CHALLENGES

- **Step 1** – Establish a detailed trail of documentation as to every consideration made and every conclusion arrived at by the Trustees. This documentation is required by the statute and is prudent in the event of subsequent litigation.
- **Step 2** – Make a determination that “all reasonable measures” to avoid insolvency have already be taken by the Trustees during the current **Critical Status** Rehabilitation process. If a determination is made that “all reasonable measures” have not already been taken, any additional measures must be identified and implemented.

STEPS AND CHALLENGES, continued

- **Step 3** - Because “all reasonable measures” does not mean that every adjustable benefit has been eliminated, nor that all future accruals of actives have been reduced to zero, nor that employer contributions levels have been increased to “unreasonable” levels; each benefit reduction/contribution increase that the Trustees have, or have not, made must be justified and documented for any application to IRS for benefit suspensions. Factors to be considered in determining whether all reasonable measures have been taken include:
 - Current and past contribution levels,
 - Levels of benefit accruals for actives,
 - Prior reduction of adjustable benefits,
 - Impact on insolvency of subsidies and ancillary benefits,

STEPS AND CHALLENGES, continued

- Compensation levels of actives as impacted by required pension contributions,
- Competitive factors affecting contributing employers,
- Impact of benefits and contributions in retaining actives,
- Impact of employer contribution increases on retention, and
- Measures undertaken by Trustees in retaining or attracting employers.



STEPS AND CHALLENGES, continued

- **Step 4** – As a first step in assessing the viability of benefit suspensions, we would recommend determining whether the Fund would satisfy the requirement of “reasonably avoiding insolvency” if all benefits eligible for suspension were reduced by the maximum amount (as low as 110% of PBGC guaranteed level). Once that determination is confirmed, we would assist the Trustees in determining levels of lesser reductions that could still accomplish the objective of completely avoiding insolvency, while not materially exceeding the levels of reduction necessary.
- *Challenge #1 – Being in **Critical and Declining Status** means the Fund’s benefit payments and expenses exceed expected employer contributions, withdrawal liability payments and investment return for the next 15 to 20 years. As a result, the first challenge will be to reduce current benefit payments to retirees and beneficiaries in payment status in order to lower the cash outflows before the Fund runs out of money.*

STEPS AND CHALLENGES, continued

- *Challenge #2 – The method for determining whether this Fund will reasonably avoid insolvency based on benefit suspensions, is different than avoiding insolvency under the current Rehabilitation Plan and is a three step process.*
 - *#1 - A “deterministic” forecast must show that the Fund’s assets are sufficient to pay benefits for each year 30 years into the future.*
 - *#2 – That same “deterministic” forecast must also show that the Fund is either 100% funded at the 30 year mark, or that neither the ratio of Fund assets to benefit payments nor Fund assets themselves has decreased in the last 5 years leading up to year 30.*
 - *#3 – A “stochastic” forecast that uses variance in investment return must show that the Fund avoids insolvency throughout the 30 year period more than 50% of the time.*

STEPS AND CHALLENGES, continued

- *Challenge #3 – The method for determining the point at which benefit suspensions materially exceed levels necessary (i.e. are “too high”) is to determine the point at which a 5% lesser reduction in benefits would fail to keep the plan solvent. Obviously this is a narrow measure and one subject to reasonable projection assumptions.*



STEPS AND CHALLENGES, continued

- **Step 5** – At this point, it is necessary that the Trustees create a written record that the plan is projected to become insolvent unless benefits are suspended even though all reasonable measures have already been taken and continue to be taken to avoid insolvency.
- **Step 6** – Once the overall “level of benefit suspensions necessary” is determined, the Trustees must determine whether the participant group as a whole should be broken down into different participant classes to receive different levels of reductions on an “equitable basis”. Attempting to achieve a truly “equitable” benefit suspension program is rife with challenges.



STEPS AND CHALLENGES, continued

➤ *Challenges –*

- 1. Identify the class of participants whose benefits cannot be reduced, or fully reduced:*
 - a. Participants age 80 or older cannot be reduced at all,*
 - b. Participants age 75 to 80 can be pro-ratably reduced in relation to the number of months until they reach age 80, and*
 - c. The disability portion of participants' retirement benefits cannot be reduced. This later criteria is complex because the disability portion of a retiree's benefit may be something less than the full accrued benefit.*

STEPS AND CHALLENGES, continued

Example: *John Smith became disabled at age 50 with 15 years of service. His immediate disability benefit payable from age 50 to age 60 was \$300/month even though his full accrued benefit payable at age 60 was \$1,500/month. In this case, the first \$300/month of his benefit due to disability retirement cannot be reduced, but the remaining \$1,200/month can be reduced.*



STEPS AND CHALLENGES, continued

2. *Should some consideration be given to participants who earned service on or after the effective date of a Rehabilitation Plan (RP) and who have already been impacted by lower benefit accruals than participants who retired prior to that date. Some such participants have been impacted more than others, for example, a participant who is still active today may have earned substantially lower benefits for the years since the RP, while those who retired prior to the RP were not impacted at all.*

3. *Participants who were not eligible to retire by the RP may have already lost the adjustable benefits of early retirement and joint & survivor subsidies that others have not. Should special consideration be given to these participants?*

STEPS AND CHALLENGES, continued

4. *Should the participants of employers who have withdrawn be treated differently than the participants of employers who actively contribute?*

NOTE: Remember that employer withdrawal liability may not equal the value of the benefits of the employer's participants.

- a. *Employers who withdrew without paying any withdrawal liability due to bankruptcy or application of the de minimis rule.*
- b. *Employers who withdrew and paid some, but not all of their full withdrawal liability.*



STEPS AND CHALLENGES, continued

c. Employers who withdrew when the Plan was overfunded and didn't owe any withdrawal liability. Even though the Plan may have been funded at the time of withdrawal, investment losses in the early 2000's and 2008 have left those participant's benefits that were once funded, to be underfunded today.

d. Employers who paid all of their withdrawal liability. Again, investment losses in the early 2000's and 2008 have left those participant's benefits underfunded.

➤ *NOTE: With respect to such participants, remember that some portion of their benefits may have been earned with an employer who may have withdrawn while other portions may have been earned with employers who are still contributing.*



STEPS AND CHALLENGES, continued

- *5. Should those participants whose benefits were enhanced above normal benefit accrual rates by provisions such as a special 25 & 30 & Out level be treated differently?*
- **Step 7** – Once the Plan is reasonably expected to avoid insolvency, the Trustees should consider whether to proceed with the benefit suspension application process.
- **Step 8** – Begin to prepare the application process to the IRS including the required level of documentation.
- **Step 9** – Appoint a retiree representative no less than 60 days prior to the date the IRS application is submitted.



STEPS AND CHALLENGES, continued

- **Step 10** – Respond to any inquiries by the retiree representative, the retiree representative’s advisor(s) and the IRS. This can occur at different points throughout the process.
- **Step 11** – Develop communications materials throughout the process for participant, local unions, employers, etc.
- **Step 12** – If IRS approves, there are certain required Notices to participants, beneficiaries, unions and contributing employers.
- **Step 13** – If approved, prepare voting ballots to be sent to all participants and beneficiaries for administration by IRS, DOL and PBGC.

STEPS AND CHALLENGES, continued

- **Step 14** – Within 2 days of submission, the IRS will advise whether the application is complete. The Plan must then provide notices to participants including individualized statements showing the impact of the suspension on each participant.
- **Step 15** – If the IRS certifies the vote results, or overrides the vote and benefit suspensions are to proceed, they will be implemented.
- **Step 16** – Annual Testing to confirm that insolvency will be avoided is required.



PART III

CONCLUSIONS



CONCLUSIONS

- The process of considering benefit suspensions is a complex one and will require the skills and historical knowledge of the Fund staff, IT provider, accountant, attorney, actuary and Trustees.
- Prior to moving forward with this process, we recommend that a full, or special Trustees meeting be scheduled to outline the objectives of the Trustees and the implementation of a plan of action.