



**Insight**

# Issues in Multiemployer Pensions: Withdrawal Liability

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## Executive Summary

- The multiemployer pension system serves over 10 million active and retired workers across 1,400 retirement plans.
- Federal law imposes a fee known as withdrawal liability on employers that withdraw from sponsoring multiemployer pension plans, but in practice, pension benefits owed to former employees of withdrawn sponsors have exceeded withdrawal liability fees.
- The congressionally chartered Joint Select Committee on Solvency of Multiemployer Pension Plans is likely to consider reforming withdrawal liability, among other policies related to multiemployer pensions.

## Introduction: The Multiemployer Pension System and Congress

Over 10 million active and retired workers are covered under about 1,400 pension plans known as multiemployer, defined-benefit plans. These are collectively bargained retirement plans funded jointly by multiple employers that provide qualifying retirees with fixed retirement benefit. Funding for these plans has deteriorated over time and a number of significant plans face insolvency. The insolvency of these plans would also swamp the federal backstop, the Pension Benefit Guarantee Corporation (PBGC).

Congress established the Joint Select Committee on Solvency of Multiemployer Pension Plans to grapple with the challenges confronting the multiemployer pension system and the projected insolvency of the federal failsafe, and to weigh appropriate federal involvement. Among the issues with which the Committee must contend is withdrawal liability.<sup>[1]</sup> When a plan sponsor decides for any number of reasons to terminate its participation in a multiemployer plan, it must pay a fee, known as withdrawal liability. Withdrawal liability is nominally designed to cover the obligations that a plan sponsor would have otherwise been required to meet to its retirees. So-called “orphan” liabilities – pension obligations to retirees from sponsors that have withdrawn – are a significant driver of the instability in the multiemployer pension system, however, which suggests that withdrawal liability is insufficient.

While that simple conclusion belies the complexity of the multiemployer pension system, the structure of withdrawal liability is a likely target for reform. The Committee has until November 30, 2018, to report recommendations to improve the solvency of the multiemployer pension system. This primer examines the design of current withdrawal liability rules and assesses considerations for reforming the current withdrawal liability regime.

## Withdrawal Liability: History and Structure

The 1980 Multiemployer Pension Plan Amendments Act (MPPAA) imposed an exit penalty, called a “withdrawal liability,” on employers who withdraw from an underfunded plan. Withdrawal liability was

introduced to prevent withdrawing employers from shifting pension obligations to the remaining employers in a plan. After a withdrawal, the plan determines whether participants' vested benefits are greater than the value of plan assets. If this is the case, the plan will calculate the withdrawing employer's share of the unfunded vested benefits based on the formula in the plan and collect it from the employer. A reduction in the requirement to contribute, including layoffs, plant closures, or changes in the collective bargaining agreement, can trigger a complete or partial withdrawal from a plan, thus resulting in the imposition of withdrawal liability. If all, or substantially all, of the contributing employers withdraw, the withdrawal is categorized as a mass withdrawal.

An employer's withdrawal liability is based on its allocated share of the total plan's unfunded vested benefits (UVBs). The amount of the employer share further depends on the date of valuation of the plan's assets and liabilities, the actuarial assumptions and methods used, and the allocation method adopted by the plan. The periodic payment amount is calculated based on the employer's historical contribution rates and contribution base units (for example hours or wages).[2] In general, the maximum amount of an annual payment is calculated by multiplying the employer's highest average annual contribution base units for any three consecutive years during most recent 10 years, by the highest contribution rate during those same 10 years.[3]

The law contains two basic types of allocation methods:

- The direct attribution method, which involves tracing UVBs attributable to the employer's workers.
- The pro rata method, which allocates liability in proportion to the employer's share of the contributions over a period of time.

Additionally, there are special provisions meant to limit the impact of withdrawal liability. These include a *de minimis* reduction adjustment, which reduces small withdrawal liability obligations and a 20-year payment cap.

An employer that withdraws does not need to pay the withdrawal liability in a lump sum. Instead, the employer may pay down its withdrawal liability obligation, with accumulated interest, through periodic payments. In addition, the employer's withdrawal liability payments are limited to 20 years. After 20 years pass, any unpaid withdrawal liability is reallocated among the remaining employers in the plan. Under a mass withdrawal, however, the 20-year cap no longer applies.

In practice, an exiting employer's actual payment is often based its ability to pay. [4] The lump sum settlement amount is usually just a percentage of the present value of the future withdrawal liability payments. In very well-funded plans, there is often no withdrawal liability associated with exiting. In plans that are moderately well-funded, the withdrawal liability is usually paid off before the 20-year cap is hit. In poorly funded plans, however, withdrawal liability payments are often limited by the 20-year cap.

### **Withdrawal Liability: Considerations for Reform**

Some employers may calculate that withdrawing from an insolvent plan and paying their current withdrawal liability is less burdensome than remaining in the plan and continuing to pay high contribution rates. An employer that intentionally withdraws from a plan expecting to pay its calculated withdrawal liability could unintentionally become part of a mass withdrawal if substantially all of the other employers in the plan withdraw within three years after the employer withdraws. The risk of being part of a mass withdrawal is that an employer may be required to pay significantly more in withdrawal liability than it would have under a regular withdrawal. In a mass withdrawal, the withdrawal liability is calculated using PBGC interest rates that are often

lower than the rates used by a plan for a regular withdrawal. In addition, reallocation liability reallocates a plan's costs of all unfunded vested benefits among all withdrawing employers and can significantly increase the amount of the plan's unfunded liability that is allocated to a withdrawn employer. And further, the 20-year cap that applies to a regular withdrawal does not apply to mass withdrawal, possibly resulting in some employers having to pay withdrawal liability for more than 20 years. For exiting employers that represent a large percentage of a plan's contribution base, the risk of subsequent mass withdrawal is particularly large because once smaller employers find out that a large employer is exiting, smaller employers have an increased incentive to withdraw so as not to be one of the last remaining employers in the plan. Unexpected and expanded withdrawal liability has the potential to lead to employer bankruptcies and deterioration of the sponsored pension plan.[5]

Ex-post, to the extent that orphan liabilities are a significant contributor to the deleterious state of multiemployer employer pension finances, the withdrawal liabilities designed to cover them have been inadequate. Simply ratcheting up withdrawal liabilities is unlikely to substantially enhance the solvency of the multiemployer pension system, however, given the conditions that might precipitate an employer's withdrawal and the potential downside risks that attach to the mass withdrawal regime.

## **Conclusion**

The fundamental challenge confronting the multiemployer pension system is underfunding of promised benefits. There are myriad reasons for this funding deficiency, and no simple policy change can quickly reverse the precarious and deteriorating finances of the system as a whole. Reform of the withdrawal liability regime, which has historically proven insufficient to offset orphan liabilities, is a reasonable step. But alone the withdrawal regime is an inadequate policy lever for the current challenge.

[1] For more on the multiemployer pension system and the Joint Select Committee, see:  
<https://www.americanactionforum.org/insight/multiemployer-pension-financing-and-federal-policy/>

[2] Employee Retirement Income Security Act of 1974 (ERISA) Secs. 4201, 4202, 4206, 4209, 4211 and 4219

[3] [https://www.ifebp.org/education/schedule/Documents/1601/P14\\_Basics\\_of\\_Withdrawal\\_Liability.pdf](https://www.ifebp.org/education/schedule/Documents/1601/P14_Basics_of_Withdrawal_Liability.pdf)

[4]  
[http://www.actuary.org/files/publications/Joint\\_Select\\_Committee\\_Multiemployer\\_Plans\\_Questions\\_for\\_Record\\_05.18](http://www.actuary.org/files/publications/Joint_Select_Committee_Multiemployer_Plans_Questions_for_Record_05.18)

[5] [https://www.uschamber.com/sites/default/files/multiemployer\\_report\\_businesses\\_and\\_jobs\\_at\\_risk\\_final.pdf](https://www.uschamber.com/sites/default/files/multiemployer_report_businesses_and_jobs_at_risk_final.pdf)