Multiemployer Plans Poised For More Assumption Rate Suits

By **Jeffrey Mamorsky** (August 17, 2020)

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Challenges to the reasonableness of pension plan actuarial assumptions are confronting corporate plan sponsors not only with regard to their own plans but also with respect to the calculation of withdrawal liability when they exit a multiemployer plan.

Since the enactment of the Multiemployer Pension Plan Amendments Act, withdrawal liability under the Employee Retirement Income Security Act has been derived by using actuarial assumptions and methods which "in the aggregate are reasonable" and "offer the actuary's best estimate of anticipated experience under the plan."[1] In this regard, ERISA provides that the actuary "may rely on the most recent complete actuarial valuation used for [minimum funding] purposes."

However, as multiemployer plans become less well funded, plan trustees have been using more conservative assumptions based on Pension Benefit Guaranty Corp. termination liability in order to increase the employer's liability in withdrawing from the plan. This has led to litigation quarreling over whether actuaries may have best estimates that differ for withdrawal liability and funding purposes.

There have been a flurry of decisions on this subject in recent months with different courts split on whether using different assumptions for different purposes can be attacked as presumptively unreasonable both in arbitration and on judicial review.

Moreover, on an important issue of first impression under the Multiemployer Pension Plan Amendments Act, the U.S. Court of Appeals for the Second Circuit has ruled that a multiemployer pension plan cannot calculate a withdrawing employer's liability based on actuarial assumptions adopted after the last day of the plan year preceding the withdrawal.

According to the Second Circuit, this anti-retroactivity rule is consistent with legislative interest and protects employers from the risk of manipulation and abuse.

D.C. District Court Upholds Different Assumptions for Funding and Withdrawal Liability

On May 22, in United Mine Workers of America 1974 Pension Plan v. Energy West Mining Company, the U.S. District Court for the District of Columbia affirmed an arbitration award requiring a company to pay more than $115 million in withdrawal liability basing its calculation on the expectation that pension assets would return about 2.75%.[2] The company argued that the plan should have used the 7.5% expected return rate it used for funding purposes which would reduce the company's liability to about $40 million.

The district court agreed with the plan deciding that there is no requirement that a pension plan calculate withdrawal liability using the same assumptions it uses when determining funding levels. And though the "huge gap" between the two figures "does give the court some pause," the court said that it is reasonable to calculate withdrawal liability using a rate that accounts for the reduced future risk an employer enjoys when it withdraws from a pension plan.

In so holding, the district court emphasized that it was not unreasonable for the plan to choose a lower withdrawal liability discount even though the company argued that the U.S. Supreme Court has held[3] that the discount rate used to calculate an employer's withdrawal liability should not differ from the discount rate used to calculate the employer's minimum funding requirements to the plan, unless there is a good reason to do so.

According to the district court, ERISA requires only that the assumptions underlying the selection of withdrawal liability discount rates be reasonable in the aggregate. ERISA does not require that the minimum funding rate and withdrawal liability discount rate be the same.

Ohio District Court Orders Plan to Recalculate Based on Funding Assumptions

On May 19, in Sofco Erectors Inc. v. Trustees of the Ohio Operating Engineers Pension Fund and the Ohio Operating Engineers Pension Fund, the U.S. District Court for the Southern District of Ohio held that a multiemployer pension plan could not use the so-called Segal blend — a weighted average of Pension Benefit Guaranty Corp. and funding rates — for a company that exited the plan.[4] The Segal blend is so named because it was originally created by the pension actuarial firm The Segal Group Inc.

The company argued that use of the Segal blend to calculate the withdrawal liability instead of the rate it used to determine its funding level for ERISA minimum funding requirements resulted in a significantly higher withdrawal liability assessment. The Segal blend is a lower rate than the rate the plan used to determine funding and resulted in a much higher withdrawal liability amount. Indeed, had the plan used the interest rate it used to determine funding, its withdrawal liability would be near zero.

Initially, the arbitrator found that the plan's use of the Segal blend was reasonable and granted the plan's motion for summary judgment. The Ohio district court concluded that use of the Segal blend was unreasonable and reversed the arbitrator's decision.

In so holding, the court emphasized that the plan actuary testified that the 7.25% rate that the plan uses to determine funding levels is based upon "a review of past experience and future expectations taking into account the plan's asset allocation and expected returns." But instead of using the rate it believed represented future expectations, it used the lower Segal blend, resulting in nearly $1 million in withdrawal liability.

Accordingly, based on the actuary's testimony and evidence presented, the district court determined that the arbitrator erred in applying the Segal blend and held that the company has shown that the 7.25% rate is mandated by ERISA.

In addition, the court said that it agreed with the company's argument that ERISA does not permit the plan to use different rates for funding and withdrawal liability. Relying on a recent opinion in National Retirement Fund v. Metz Culinary Management discussed below,[5] the court reasoned that the "opportunity for manipulation and bias is particularly great where funds use different interest rate assumptions for withdrawal liability and minimum funding purposes."

This ruling is perhaps more significant because under the Multiemployer Pension Plan Amendments Act, arbitrators' rulings are entitled to a rebuttable presumption of correctness that the employer must overcome.

It is important to note that this is not the first instance of a district court overturning the Segal blend. On March 26, 2018, in New York Times Co. v. the Newspaper and Mail Deliverers'-Publishers' Pension Fund, the U.S. District Court for the Southern District of New York,[6] found that the Segal blend violated ERISA and that the actuary's best estimate of anticipated experience under the plan required an interest rate assumption of 7.5%, the rate used for funding purposes, rather than the 6.5% interest rate produced by the Segal blend.

On the other hand, in Manhattan Ford Lincoln Inc. v. UAW Local 259 Pension Plan in 2018, the U.S. District Court for the District of New Jersey[7] upheld an arbitrator's ruling that using a plan's funding assumption is not required to determine withdrawal liability. In so ruling, the New Jersey district court determined that the employer had failed to prove that the pension plan's use of the Segal blend in calculating withdrawal liability was not reasonable.

Notably, use of the 7.5% interest rate for funding purposes would have resulted in no withdrawal liability.

Second Circuit Prohibits Retroactive Changes to Withdrawal Liability Assumptions

In a decision of first impression, the Second Circuit held in January in National Retirement Fund v. Metz Culinary Management that the interest rate assumption used to calculate withdrawal liability is the rate that was in effect on the last day of the plan year preceding the year of the employer's withdrawal from a multiemployer pension plan.[8]

In so holding, the Second Circuit rejected the plan actuary's decision to use a lower discount rate adopted after the measurement date that had the effect of substantially increasing the amount of the employer's liability. The court emphasized that retroactive changes to the actuarial methods and assumptions used to calculate withdrawal liability are inconsistent with the legislative history of ERISA Section 4214, which requires the fund to provide advance notice to employers of any plan rules and amendments that affect withdrawal liability.

Furthermore, the Second Circuit held that absent any change to the previous plan year's assumption made by the measurement date, the interest rate assumption in place from the previous plan year will roll over automatically.

According to the Second Circuit, the plan's former actuary used a 7.25% interest rate assumption which would have resulted in withdrawal liability of $254,644, whereas the current actuary reduced the interest rate assumption for purposes of withdrawal liability from 7.25% to approximately 3.25% resulting in withdrawal liability of $997,734. The arbitrator held the plan's retroactive application of the discount rate to calculate withdrawal liability was improper.

The Southern District of New York vacated the arbitrator's decision holding that ERISA does not require actuaries to make withdrawal liability assumptions by the measurement date.

On appeal, the Second Circuit determined that despite the parties use of "copious amounts of ink in argument" the issue is whether a fund may select an interest rate assumption after the measurement date and retroactively apply that assumption to withdrawal liability calculations.

In this instance, the Second Circuit said interest assumption on the measurement date was 7.25%. The fund's decision to apply a changed assumption rate retroactively so as to increase withdrawal liability is violative of ERISA.

According to the Second Circuit, in the context of multiemployer pension plans, interest rate assumptions cannot be altered daily and must have a degree of stability. Indeed, the court said, the plan itself used the 7.25% rate for several years and its annual reports to the government reflect the ongoing rollover.

The Second Circuit emphasized that ERISA Section 4214 imposes a notice requirement on multiemployer funds for any plan rule or amendment with respect to withdrawal liability. The legislative history demonstrates that this provision was designed to protect employers from the retroactive application of rules relating to the calculation of withdrawal liability.

The Second Circuit concluded that the assumptions and methods used to calculate the interest rate assumption for purposes of withdrawal liability must be those in effect as of the measurement date. Absent a change by the plan actuary before the measurement date, the existing assumptions and methods remain in effect.

Were it otherwise, the selection of an interest rate assumption after the measurement date would create significant opportunity for manipulation and bias, the court said.

Continuing Challenges

Multiemployer plans are in crisis mode doing their best to avoid insolvency. This has led to the use of more conservative actuarial assumptions for withdrawal liability.

The majority of multiemployer plans use the Segal blend, which was developed shortly after enactment of the Multiemployer Pension Plan Amendments Act. However, in the early 1980s Pension Benefit Guaranty Corp. interest factors were higher than plan funding assumptions and using a blended rate rather than pure funding assumptions benefited withdrawing employers.

The opposite has been the case for many years and today Pension Benefit Guaranty Corp. interest factors are less than 2%, which has led to employers challenging withdrawal liability for plans using anything other than pure funding assumptions.

As the Supreme Court has pointed out, the statutory requirement of "actuarial assumptions and methods which in the aggregate are reasonable" is identical for both withdrawal liability[9] and funding purposes[10] and "using different assumptions [for different purposes] could very well be attacked as presumptively unreasonable both in arbitration and on judicial review."[11]

Parties in every recent withdrawal liability case have cited this Supreme Court decision as authority with mixed results. On May 22, the D.C. district court decided that there is no requirement that a plan calculate withdrawal liability using the same assumptions it uses for funding purposes.

Although the court was sympathetic to the huge gap between the two figures it concluded that it was not unreasonable for the plan actuary to adjust the discount rate down to account for the absence of future risk for the withdrawing employer.

On the other hand, a few days earlier, the Southern District of Ohio concluded that the plan's use of the Segal blend rather than the rate it used to determine funding was unreasonable. It based its decision on the plan actuary's testimony that the plan's funding rate is based on both a review of past experience and future expectations and therefore determined that the plan was in error using the Segal blend rather than the funding rate which the actuary believed represented future expectations.

The court pointed out that, although it is not unlawful to use different rates in different contexts, here there are legal grounds to find that the plan's use of the Segal blend rather than the plan's funding discount rate for withdrawal liability purposes was erroneous. In so holding, the court said it agreed with the company's argument that ERISA does not permit the plan to use different rates for funding and withdrawal liability.

The court's reasoning was based to a great extent on the Supreme Court's admonition that the opportunity for manipulation is particularly great where plans use different rate assumptions for withdrawal liability and funding purposes.

You should be prepared for continuing challenges unless your multiemployer plan is using the same assumptions for funding and withdrawal liability purposes. If it is not, it is important that you consider justifying different withdrawal liability assumptions with an independent actuarial assumption review and opinion.

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[1] ERISA Section 4213(a).

[2] United Mine Workers of America 1974 Pension Plan v. Energy West Mining Company, 2020 WL 2615536, District of Columbia District Court (May 22, 2020).

[3] Concrete Pipe & Products v. Construction Laborers Pension Trust, 508 U.S. 62 (1993).

[4] Sofco Erectors Inc. v. Trustees of the Ohio Operating Engineers Pension Fund and the Ohio Operating Engineers Pension Fund, Case No. 2:19-cv-2238, United States District Court, S.D. Ohio, Eastern Division, May 19, 2020.

[5] Nat'l Ret. Fund v. Metz Culinary Mgmt., 2020 U.S. App. LEXIS 4, 13-14 (2d Cir. 2020), citing Concrete Pipe & Prods. v. Constr. Laborers Pension Trust, 508 U.S. 602 (1993).

[6] New York Times Company v. the Newspaper and Mail Deliverers '-Publishers ' Pension Fund, 303 F. Supp. 3d 236.

[7] Manhattan Ford Lincoln, Inc. v. UAW Local 259 Pension Plan, 333 F. Supp 3d 236 (D.N.J. appeal dismissed, 2018 W2 10759132 (3d Cir. 2018).

[8] National Retirement Fund v. Metz Culinary Management, Inc., No. 17-1211, 2020 WL 20524 (Jan. 2, 2020).

[9] ERISA Section 4213 (a)(1).

[10] ERISA Section 302 (c)(3).

[11] 508 U.S. 633 (1993).