THE SAVITZ ORGANIZATION

Memo

October 14, 2003

To: Board of Trustees – Central PA Teamsters Pension Fund

From: William P. Bishop, FCA

Subject: **Withdrawal Liability Considerations**

This memo addresses two items related to the CPAT DB Plan's allocation of withdrawal liability that, if adopted, could be used as an enticement for new employers to join the Plan, which would contribute to its long-term solvency and growth:

- Free-look
- The presumptive method

Free Look

An employer is not liable for withdrawal liability from a multiemployer plan if the free-look rule applies[1] and if the "free look" employer:

1. had an obligation to contribute to the plan for no more than five years;
2. was required to make contributions to the plan for each of the five years preceding withdrawal in an amount equal to less than two percent (2%) of the sum of all employer contributions made for that year (*about $1.28 million per year in the CPAT Plan*); and
3. has never before avoided withdrawal liability through the application of this exception.

The free look rule applies only if:

1. the plan does not primarily cover building and construction industry employees;
2. the plan is amended to provide that the free look applies;
3. the plan provides or is amended to provide that the IRC §411(a)(3)(E) reduction for the cessation of contributions under a multiemployer plan applies to the withdrawing employer's employees[2]; and

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1. In the unlikely event of a mass withdrawal, "free look" employers are liable for reallocation liability. The PBGC did not completely excuse free look employers from mass withdrawal liability because Congress determined that the amount of unfunded vested benefits of a plan experiencing a mass withdrawal had to be allocated among all withdrawing employers.
2. If affected employees are credited with past service and their employer withdraws under the free look rule, then the employees lose their past service credit. They would not lose their accrued benefits so long as the employer contributed for exactly five years (less, and they are not vested; more, and the employer will not qualify for free look).

4. the ratio of: (a) plan assets for the plan year preceding the first plan year for which the employer was required to make contributions, to (b) benefit payments made during that plan year, was at least 8 to 1[3].

PBGC Approval for Adopting the Free Look – The PBGC has approved, as a class, all plan amendments that satisfy the requirements set forth for permitting small, short-term contributors to withdraw completely or partially from a plan without incurring any liability. Thus, plans may adopt such amendments without obtaining the specific prior approval that would otherwise be required.

Rolling-Five Method vs. Presumptive Method

The amount of unfunded vested benefits (UVBs) may be allocated to a withdrawing employer for calculating withdrawal liability using either of several methods. The four basic statutory methods provided under ERISA §4211 are the:

- Presumptive method,
- Modified presumptive method,
- Rolling-five method, and
- Direct attribution method

Rolling-Five Method – The CPAT DB Plan currently uses this method, under which UVBs allocable to a withdrawing employer are equal to the product of:

1. the UVBs as of the end of the plan year before the plan year in which the employer withdraws (minus the value of all reasonably collectible outstanding claims for withdrawal liability against employers who withdrew before that year), multiplied by:
2. a fraction: (a) whose numerator is the total amount of the employer's contribution obligations for the last five plan years ending before its withdrawal, and (b) whose denominator is the total amount contributed by all employers during that time, decreased by any amount contributed during those plan years by employers who withdrew within that span.

> Because the CPAT Plan's entire UVBs are allocated in one pool, the rolling-five method will immediately allocate a portion of UVBs to a new contributing employer, even though the new employer is responsible for little or no vested benefits. This can be a significant detriment to the recruitment of new employers into the CPAT Plan, which had over $247 million in UVBs as of December 31, 2002.

3. This requirement would need to be monitored each year, but for 2003 the plan's actuarial value of assets will exceed 8 times the 2003 benefit payments.

Presumptive Method – To encourage new employers to join the Plan, the trustees may want to consider adopting the presumptive method, where the UVBs allocable to a withdrawing employer would be equal to the sum of the employer's proportional share of:

1. the unamortized amount[4] of the Plan's UVBs at the end of the plan year before the presumptive method was adopted (e.g., December 31, 2003, if first adopted in 2004);
2. the unamortized amount[4] of the change in the Plan's UVBs for plan years ending after the new method was adopted; and
3. the unamortized amount[4] of any reallocated UVBs (e.g., uncollectible amounts or de minimis offsets for withdrawal liabilities under $150,000).

An employer's “proportional share” of the unamortized amount of items 1-3 above is the product of such amount, multiplied by a fraction:

- whose numerator is the sum of the plan contributions required for the year in which the item arose and for the four preceding plan years, and
- whose denominator is the sum of all contributions made by employers with obligations for the plan year in which the change arose, for that plan year and the preceding four (reduced by the contributions made in those years by employers who had withdrawn from the plan in the plan year in which the change arose).

If the result of the above calculation is negative, the UVBs allocable to the employer equal zero.

> The presumptive method will not allocate to a new employer any pool of UVBs that existed before the employer participated in the plan. As a result, a new employer will incur far less withdrawal liability under the presumptive method than under the rolling-five method. This is particularly important to a larger employer who cannot take advantage of the free look.

Other Considerations: Sale of Assets Exception – The withdrawal liability of a purchaser of assets for which the “sale of assets” exception applies to the seller's withdrawal liability under ERISA §4204 is determined:

- as if the purchaser had been required to contribute, in the year of the sale and the four plan years preceding it,
- the amount the seller was required to contribute during those same five plan years.

In other words, the contributions made by the seller during the years prior to such five-year period are disregarded for purposes of allocating UVBs.

4. The “unamortized amount” of any UVB pool is the initial amount of those benefits, reduced by five percent (5%) of that amount for each succeeding plan year.

Under the rolling-five method, this has no effect on how the buyer's withdrawal liability differs from what would have been the seller's withdrawal liability if not for the §4204 exception. However, under the presumptive method, §4204(b)(1) would result in the nonattribution of all, or a substantial portion, of the seller's most important contribution history, since the most significant pool of UVBs in the CPAT DB Plan would be the initial amount.

Other Considerations: Change in Size or Amount of Contributions for an Existing Employer – Under the rolling-five method, if a contributing employer's proportional share of contributions increases/(decreases) over time, its share of UVBs will increase/(decrease) in at similar rate. However, under the presumptive method, such a change would not affect the pools of UVBs prior to the change in the employer's proportional share of contributions.

> Relative to the rolling-five method, the presumptive method will generally not penalize an employer who increases its contribution base or its proportional share of contributions to the plan. Similarly, the presumptive method will generally not reward an employer who decreases its contribution base or its proportional share of contributions to the plan as much as the rolling-five method.

PBGC Approval for Adopting the Presumptive Method – The plan would submit a request for approval of the presumptive method to the PBGC as soon as practicable after the adoption of the amendment. The request must contain:

- The date the amendment was adopted.
- A copy of the amendment, setting forth the full text of the allocation method.
- The allocation method that the plan currently uses and a copy of the plan amendment that adopted the method.
- A statement certifying that notice of the adoption of the amendment has been given to all employers that have an obligation to contribute under the plan and to all employee organizations that represent employees covered by the plan.

The PBGC also reserves the right to request any other information that it deems necessary for the review of the new allocation method.