October 2014

MULTIEMPLOYER ALERT
Update on Issues Affecting Taft-Hartley Plans

The new ASOP 27 – What is the impact on multiemployer plan funding?

The Actuarial Standards Board (ASB) has approved a revised version of Actuarial Standards of Practice (ASOP) No. 27, *Selection of Economic Assumptions for Measuring Pension Obligations*. The new standard is effective for any actuarial work product with a measurement date on or after September 30, 2014. For a calendar year plan, this means the new standard will first apply to the 2015 actuarial valuation. The ASB indicates that this new standard "is intended to accommodate the concepts of financial economics as well as traditional actuarial practice."

Economic assumptions covered by ASOP 27 include the investment return, discount rate, inflation, postemployment benefit increases, compensation increases, and any other related assumptions. The general process that must be followed by the actuary in developing economic assumptions is: (a) identify the components of the assumption, (b) evaluate the relevant data, (c) consider factors specific to the measurement and other general factors, and (d) select a reasonable assumption. Relevant data could include both recent and long-term historical data, but undue weight is not to be given to recent experience. Adjustments may be made to allow for the chance of an adverse deviation or if there are plan provisions that are hard to value.

The greatest impact of the revised ASOP may appear in the development of multiemployer pension plan liabilities through its effect on the actuary's selection of the investment return assumption.

Prior to the revision, ASOP 27 used a "best-estimate" range to determine reasonableness. Under this standard, an assumption was considered reasonable as long as it was selected from a probabilistic range in which it was likely to fall. For example, in a stochastic projection of asset returns, an assumption within the 25th to 75th percentile of projected returns over an appropriate period might have been deemed reasonable even though the median is actually the precise measure of the best estimate. In the current extended period of low inflation and low interest rates, some actuaries have in practice selected an investment return assumption well above the median return. Using a higher investment return assumption produces lower plan liabilities.

Under the revised standard, an assumption is considered reasonable if (a) it is appropriate for the purpose of the measurement; (b) reflects the actuary's professional judgment; (c) takes into account relevant historical and current economic data; (d) reflects the actuary's estimate of future experience, the actuary's observation of estimates inherent in market data, or a combination thereof; and (e) *has no significant bias* (although a margin for adverse deviation may be intentionally incorporated). Under these more subjective criteria, an actuary may find it more difficult to justify an investment return assumption significantly greater than the median projected return. This could lead to an overall lowering of assumed interest rates used in valuing benefits for multiemployer pension plans, with a corresponding increase in liabilities. For a typical pension plan, depending upon the makeup of the plan's population, lowering the interest rate used to value benefits by one percentage point could generate a 10% to 20% increase in plan liabilities. These higher liabilities will likely lead to:

1. Higher funding requirements for a given level of benefits
2. Higher withdrawal liability amounts (if funding assumptions are used in the withdrawal liability calculations)
3. The "tightening up" of rehabilitation and funding improvement plans that were originally developed using a higher interest assumption

As practice emerges under the new standard, Milliman will continue to update you on its impact.

If you have any questions, please contact your Milliman consultant.

Multiemployer Alert: Update on Issues Affecting Taft-Hartley Plans is intended to provide information and analysis of a general nature. Application to specific circumstances should rely on separate professional guidance.

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