DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

November 10, 2016

Board of Trustees, Teamsters Local 469 Pension Fund
3400 Highway 35, Suite 8
Hazlet, NJ 07730-1247

Dear Mr. Voelker and the Board of Trustees:

On March 30, 2016, you submitted an application to the Secretary of the Treasury (Secretary or Treasury) on behalf of the Board of Trustees of the Teamsters Local 469 Pension Fund (Plan). The application you submitted (Application) requests approval to reduce benefits under the Multiemployer Pension Reform Act of 2014 (Kline-Miller or Act).

As Special Master, appointed by the Secretary, I am writing to notify you of Treasury's decision to deny the Application because the proposed suspension fails to satisfy the statutory criteria for approval.

In my role as Special Master, I have reviewed the Application under the terms of Kline-Miller, its implementing regulations, and other applicable law. I also have reviewed the comments received on the Application from organizations and individuals.

Under the Act, Treasury, in consultation with the Pension Benefit Guaranty Corporation (PBGC) and the Secretary of Labor (DOL), must approve an application upon finding that the plan is eligible for the benefit suspensions and has satisfied the applicable statutory requirements.[1] The Act requires, among other things, that the Application demonstrate that the proposed benefit suspensions are reasonably estimated to allow the plan to avoid insolvency.[2] Treasury cannot approve an application under Kline-Miller unless the proposed benefit suspensions would reasonably ensure the plan's long-term solvency. As described further below, Treasury does not find that the Plan's proposed benefit suspensions are reasonably estimated to allow the Plan to avoid insolvency.

Specifically, after reviewing the Application and consulting with PBGC and DOL, Treasury has determined that the suspensions described in the Application fail to satisfy the requirement set forth in Kline-Miller "that the proposed benefit suspensions, in the aggregate, be reasonably estimated to achieve, but not materially exceed, the level that is necessary to avoid insolvency",

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[1] Code§ 432(e)(9)(G)(i); 29 U.S.C. § 1085(e)(9)(G)(i).

[2] "Limitations on Suspension-Any suspension of benefits made by a sponsor pursuant to this paragraph shall be subject to the following limitations: ... Any suspension of benefits in the aggregate ... shall be reasonably estimated to achieve ... the level that is necessary to avoid insolvency . . . ." Code§ 432(e)(9)(D)(iv); 29 U.S.C. § 1085(e)(9)(D)(iv). In the interest of simplicity, all citations below to Kline-Miller will refer only to the Internal Revenue Code even though Treasury's findings and conclusions have been made under both the Internal Revenue Code and the Employee Retirement Income Security Act of 1974, as amended.

because the zero-takeup assumption regarding spousal survivor benefits and the investment return assumption used for this purpose are not reasonable. Code§ 432(e)(9)(D)(iv).

Treasury's key findings are described below.

FINDINGS

Kline-Miller requires the Secretary of the Treasury to approve, in consultation with PBGC and DOL, an application for suspension of benefits "upon finding that the plan is eligible for the suspensions and has satisfied the criteria of subparagraphs (C), (D), (E), and (F)" of section 432(e)(9) of the Internal Revenue Code (Code), as amended by Kline-Miller.[3] The Application fails to satisfy the criteria of subparagraph (D)—which requires that benefits be reasonably estimated to avoid insolvency—as further described below.

Requirement that Suspension Be Reasonably Estimated to Avoid Insolvency

Section 432(e)(9)(D) of the Code provides that:

> [a]ny suspensions of benefits under a plan, in the aggregate . . . , shall be reasonably estimated to achieve, but not materially exceed, the level that is necessary to avoid insolvency.

Pursuant to the regulations implementing this provision, an applicant must use actuarial projections to demonstrate that a suspension satisfies this requirement. One type of required actuarial projection is a deterministic projection of cash flows, under which the plan's asset balance is projected forward using assumptions regarding the amounts of money coming into the plan (for example, contributions, withdrawal liability payments, and investment returns) and the amounts going out of the plan (for example, benefit payments and administrative expenses). The period over which an applicant must demonstrate that it satisfies this requirement is at least 30 years, and is lengthened for such time as is necessary for the plan to demonstrate that its solvency ratio[4] and available resources[5] do not decline during the last five years of the period. In this case, the Plan's period for demonstrating solvency ends in 2060, which results in a 45-year solvency projection period.

The regulations require that each of the actuarial assumptions and methods, as well as the combination of actuarial assumptions and methods, used for the required actuarial projections be reasonable, taking into account the experience of the plan and reasonable expectations.[6] In evaluating whether the assumptions and methods used in the application are reasonable, Treasury

[3] Code § 432(e)(9)(G)(i).

[4] A plan's solvency ratio is defined at § 1.432(e)(9)-1(d)(5)(ii)(B) as the ratio of the plan's available resources (as defined in § 418E(b)(3) of the Code) for the plan year to the scheduled benefit payments under the plan for the plan year.

[5] A plan's available resources are defined under § 418E(b)(3) as the plan's cash, marketable assets, contributions, withdrawal liability payments, and earnings, less reasonable administrative expenses and amounts owed for such plan year to PBGC under section 4261(b)(2) of ERISA.

[6] 26 C.F.R. § 1.432(e)(9)-1(d)(5)(iv)(B).

has referred to guidance provided by the Actuarial Standards of Practice (ASOPs), which are the principal professional standards that apply to the actuarial profession.[7]

The ASOPs require that historical and current demographic and economic data relevant as of the measurement date be taken into account in selecting actuarial assumptions and methods, and the ASOPs further require that the assumptions have no significant bias. The ASOPs and regulations also require that each of the assumptions or methods be appropriate for the purposes of the measurement (which means, among other things, that factors specific to the measurement must be taken into account). In this case, the measurements are the cash flow projections that are required under Kline-Miller. In addition, the actuary must consider the materiality of the assumptions and the balance between the benefits of using refined assumptions (that is, assumptions that are based upon more extensive and specific study and research) and the cost of using those refinements.

Treasury has concluded that two of the assumptions used for the actuarial projections in the Application—the assumption regarding the election of spousal survivor benefits and the investment return assumption—are not reasonable.

The Plan's Zero-Takeup Assumption Regarding Spousal Survivor Benefits Is Not Reasonable

Under the terms of the Plan and applicable law, benefits to an unmarried participant must be paid in the form of a life annuity (sometimes referred to as a single-life annuity), and benefits to a married participant must be paid in the form of a joint-and-survivor annuity, unless these default forms of benefit are waived. A single-life annuity provides a monthly payment to the participant for his or her lifetime; a joint-and-survivor annuity pays a monthly benefit to the participant for his or her lifetime and then pays a continuing benefit to the participant's surviving spouse for the remainder of the spouse's lifetime.

In the case of a joint-and-survivor annuity, the monthly amount paid to the participant may be actuarially reduced to fully account for the additional amount that is expected to be paid to the participant's surviving spouse, such that the value of the joint-and-survivor annuity is equal to the value of the single-life annuity that the participant would be entitled to receive if he or she were unmarried. Alternatively, the monthly amount paid to a participant under a joint-and-survivor annuity may be reduced by a lesser amount (or not at all), such that the value of the joint-and-survivor annuity is greater than the value of the single-life annuity. If the value of the joint-and-survivor annuity is greater than the value of the single-life annuity, the joint-and-survivor annuity is said to be subsidized. The joint-and-survivor annuity under the Local 469 Plan is slightly subsidized.

In the case of a married participant, the participant may waive the joint-and-survivor benefit (and receive a different form of benefit, such as a single life annuity) only if the participant's spouse consents to the alternative form of payment. The consent of the spouse must be in writing and must be witnessed. Because these requirements must be satisfied in order to opt out of the default, and in view of the protection offered by a survivor benefit paying lifetime benefits to the

[7] In this case, the relevant ASOPs are primarily ASOP numbers 4, 27, and 35.

participant's spouse if the spouse survives the participant, most married plan participants receive their benefits in the form of a joint-and-survivor annuity. The Plan's own experience is that over 70 percent of participants receive a joint-and-survivor annuity.

In its Application, the Plan assumes that 80 percent of all participants who have not commenced their benefits are married, and its cash flow projections reflect the further assumption that 100 percent of the married participants will choose to waive their subsidized joint-and-survivor annuities and receive less valuable single-life annuities. This assumption is not reasonable because it:

1. does not adequately take into account relevant historic and current demographic data;
2. has a significant bias; and
3. is not appropriate for the purpose of the measurement (the cash flow projections relating to proposed benefit suspensions under Kline-Miller).

The Application's Zero-Takeup Assumption Fails to Take into Account Relevant Current and Historical Demographic Data

As noted above, the Application assumes that 80 percent of participants who have not commenced their benefits are married. However, the projections in the Application also reflect an assumption that none of these participants will receive a joint-and-survivor annuity. This zero-takeup assumption—that every one of the married participants and their spouses will elect against the default and decline the joint and survivor annuity—is contradicted by the common experience in pension plans, as noted, including this Plan's own experience that over 70 percent of participants receive a joint-and-survivor annuity. Moreover, there is reason to believe that the take up rate for joint-and-survivor annuities would be even higher if the proposed suspension were approved.[8]

The Zero-Takeup Assumption Regarding Spousal Survivor Benefits Has a Significant Bias

The Application's assumption in the cash flow projections regarding the election of survivor benefits has a significant bias because it has the effect of underestimating the amounts that the Plan will pay to participants and beneficiaries. By assuming that all benefits will be paid in the form of single-life annuities, the Plan ignores the additional cost associated with paying the joint-and-survivor annuities (which, as noted, are subsidized). When the Plan recalculated its

[8] Under Kline-Miller, benefits to a participant or beneficiary cannot be reduced to less than 110 percent of the benefit amount that is guaranteed by the PBGC. Further, under PBGC rules, the PBGC guarantees the same monthly amount for a participant whether the participant's benefit is paid in the form of a single-life annuity or a joint-and-survivor annuity. As a result, joint-and-survivor annuity benefits are relatively more protected than single-life annuity benefits under a suspension because the monthly joint-and-survivor payments are already lower to begin with, meaning that the size of a cut in monthly joint-and-survivor annuity benefits will be less than the size of a cut in monthly single-life annuity benefits. (For example, if before a suspension a single-life annuity would pay $1,500 a month, a joint-and-survivor annuity would pay $1,400, and the 110-percent PBGC guarantee is $1,200 a month, then the reduction of benefits under the suspension could be up to $300 a month if the participant were to elect a single-life annuity, but could only be up to $200 a month if the participant were to take a joint-and-survivor annuity; the cuts to a joint-and-survivor benefit would be up to $100 a month less than the cuts to a single-life annuity benefit.) Thus, participants would benefit more from the Kline-Miller PBGC-based limitation by taking a joint-and-survivor annuity and would therefore be more likely to take a distribution in that form.

solvency projection assuming that 80 percent of participants elect a joint-and-survivor annuity—a reasonable assumption given the Plan's experience and the likely possibility that more participants would choose to take joint-and-survivor annuities—the Plan was projected to become insolvent within the solvency projection period.

The Zero-Takeup Assumption Regarding Spousal Survivor Benefits Is Not Appropriate for the Purpose of the Measurement

In evaluating whether actuarial assumptions are appropriate for the purpose of a measurement, the ASOPs provide that factors specific to the measurement must be taken into account. As noted above, in this case the purpose of the measurement is a cash flow projection to demonstrate that a proposed benefit suspension under Kline-Miller is reasonably estimated to achieve, but not materially exceed, the level that is necessary for the Plan to avoid insolvency. Accordingly, the following factors are relevant to this cash flow projection and should be taken into account in selecting an assumption about participant election of survivor benefits:

- that a participant's or beneficiary's loss of benefits (once reduced pursuant to a suspension) is permanent—amounts reduced will not be returned; and
- that the amount of the suspension cannot easily be (and will not automatically be) increased or decreased in a later year if the plan's actual experience proves to be different than projected.

These factors indicate the serious and significant impact of the benefit suspension on participants and beneficiaries. Given this impact, the Plan should have used more refined assumptions regarding the election of spousal survivor benefits because those refinements would have produced materially different results and would not have been costly for the Plan to develop or implement.

Based on the foregoing, Treasury has determined that the assumption regarding the election of survivor benefits by participants is not reasonable, and therefore the proposed suspension does not satisfy the statutory requirement that it be reasonably estimated to avoid insolvency.

The Investment Return Assumptions Are Not Reasonable

The Application uses a 7.25 percent annual investment rate of return assumption for the entire 45-year solvency projection period. This assumption is not reasonable because it:

1. does not adequately take into account relevant current economic data (that is, appropriate investment forecast data);
2. has a significant bias in that it is significantly optimistic;
3. is not appropriate for the purpose of the measurement (cash flow projections relating to proposed benefit suspensions under Kline-Miller), taking into account the Plan's negative cash flows and other factors.

The Investment Return Assumptions Do Not Take into Account Relevant Current Economic Data

The investment return assumptions used in the Application do not adequately take into account relevant current economic data. Relevant current economic data (including near-term current investment forecast data for each asset class in which the Plan is projected to make investments) must be reviewed to determine whether refined investment return assumptions would be expected to produce materially different results.

A review of relevant current economic data clearly demonstrates that refined investment return assumptions that take into account appropriate investment forecast data regarding expected near-term rates of return would be expected to produce materially different results. Treasury used the 2015 Survey of Capital Market Assumptions, developed by Horizon Actuarial Services, as a source of relevant current economic data.[9] The 2015 Horizon Survey is an annual report aggregating the investment forecasts of 29 investment advisors that is widely used in evaluating the capital market assumptions utilized by multiemployer defined benefit plans. Applying the Horizon Survey's results to the plan's target portfolio, 6.53 percent is the average expected geometric return over the next 10 years, compared to the Plan's assumption of 7.25 percent. The Plan's assumption of 7.25 percent exceeds the Horizon Survey's 75th percentile rate of return over the next 10 years, which is 7.17 percent.[10]

The Investment Return Assumptions Have Significant Bias

The investment return assumptions used in the Application do not satisfy the requirement that assumptions have no bias outside of narrowly specified circumstances. The assumptions are significantly optimistic, as evidenced by the available relevant investment return forecast data in the Horizon Survey described above, and the assumptions have a material effect on the actuarial projections in the Application. For example, even reducing the Plan's assumed investment return for only the first three years of the solvency projection period (2016, 2017, and 2018) to the 6.53 percent expected under the Horizon Survey and maintaining the Plan's assumed 7.25 percent investment return for the remaining 42 years would cause the Plan to become insolvent during the solvency projection period. Similarly, if the 6.53 percent rate of return were assumed for the first 10 years, it would be necessary to assume an 8.65 percent rate of return for the following 35 years in order for the Plan to avoid insolvency prior to the end of the solvency projection period in 2060; an 8.65 percent rate of return exceeds the 75th percentile return for years 11 through 45 produced by applying the Horizon Survey results.

The Investment Return Assumptions Are Not Appropriate for the Purpose of the Measurement

To be appropriate for the purpose of the measurement, investment return assumptions, like demographic assumptions, must be selected in a manner that takes into account factors specific to the measurement. In addition to the factors described above for selecting assumptions relating to the election of survivor benefits (which indicate that more refined assumptions should have been used given the serious and significant impact of the benefit suspensions on participants and beneficiaries), the Plan should have taken into account the greater impact of asset returns during

[9] At the time the Application was submitted, the most recent survey data available was the 2015 Horizon Survey.
[10] The average rates of return for the portfolio in this paragraph are geometric averages (used as the basis for the assumption for the deterministic projections).

the earlier years of the cash flow projections when selecting an investment return assumption. Asset returns during the early years have a greater impact on the Plan's cash flow projections because the Plan is projected to have more assets during the earlier years of the projections than during the later years (which is always the case for a plan with dwindling assets that is projected to become insolvent in the near term); the same percentage gain or loss has a greater impact if it occurs when asset levels are higher, which is the case in the early years, than when asset levels are lower, which is the case in the later years.

Based on these factors, the investment return assumptions for purposes of the cash flow projections in the Application must be developed in a refined manner that reflects and gives appropriate weight to near-term expected rates of return. For this purpose, it is not appropriate to develop investment return assumptions based solely on the time-weighted average expected returns over the long term or based on the assumptions used for other purposes (such as for purposes of determining a plan's minimum funding requirement) because doing so produces materially different results than use of a refined assumption selected in a manner that takes into account the purposes of this measurement.

Based on the foregoing, Treasury has determined that the investment return assumptions are not reasonable, and therefore the proposed suspension does not satisfy the statutory requirement that it be reasonably estimated to avoid insolvency.

Additional Concerns with the Application

The Application also included the following assumptions and methods that may not be reasonable for the purpose of the measurement but that are unlikely to have a material impact on the outcome of the cash flow projections:

- The assumption that active participants who become disabled will wait until age 65 to commence benefits. The most reasonable assumption is that disabled participants who are no longer earning wages and are likely to have a shorter life expectancy would commence benefits when they are eligible to do so.

- The assumption that all participants who are past normal retirement age but have not yet retired will retire immediately.

- For participants who are likely to retire when they first become eligible for an unreduced early retirement benefit upon completing 30 years of service, the assumption that benefit commencement will begin on the 30th anniversary of plan participation, which does not take into account that some participants may have partial years of service and thus their eligibility for this benefit would be delayed.

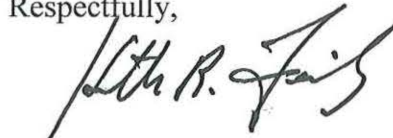
- The assumption that the mortality rates of plan participants are those of a person two years older than the participant's actual age (i.e., ages are set forward two years).

- The projections did not take into account the proposed suspension of accruals earned during 2015.

CONCLUSION

The Application fails to meet the requirements of Kline-Miller for the reasons described above. This notification letter will be made public in order to inform plan participants and beneficiaries of the outcome of Treasury's review.

Respectfully,



Kenneth R. Feinberg
Special Master