DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

August 11, 2020

Christopher J.G. Brockmeyer
Raymond M. Hair, Jr.
Board of Trustees
American Federation of Musicians & Employers Pension Fund
Fourteen Penn Plaza – 12th Floor
New York, NY 10122

Re: American Federation of Musicians and Employers Pension Fund Application for Benefit Suspension

Dear Mr. Brockmeyer, Mr. Hair, and the Board of Trustees:

On December 30, 2019, you submitted an application to the Secretary of the Treasury (Secretary or Treasury) on behalf of the Board of Trustees of the American Federation of Musicians & Employers Pension Fund (Fund). The application you submitted (Application) requests approval to reduce benefits under the Multiemployer Pension Reform Act of 2014 (MPRA).

Treasury has reviewed the Application under the terms of MPRA and MPRA's implementing regulations. Treasury also has reviewed the comments received on the Application from organizations and individuals.

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.

Under MPRA, 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] After reviewing the Application and consulting with PBGC and DOL, Treasury has determined that the suspension described in the Application fails to satisfy the requirement set forth in MPRA "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."[2] Specifically, Treasury has determined that the mortality rate assumption and the new entrant assumption are not reasonable under the standards in the regulations. Treasury's key findings are described below.

FINDINGS

MPRA requires the Secretary of the Treasury to approve an application for a suspension of benefits, in consultation with PBGC and DOL, "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 MPRA.[3]

[1] Code§ 432(e)(9)(G)(i).
[2] Code§ 432(e)(9)(D)(iv).
[3] Code § 432(e)(9)(G)(i).

As further described below, the Application fails to satisfy the criteria of subparagraph (D) of Code § 432(e)(9) because it does not comply with the limitation of clause (iv) of subparagraph (D), which requires that "[a]ny suspensions of benefits, in the aggregate . . . shall be reasonably estimated to achieve, but not materially exceed, the level that is necessary to avoid insolvency."[4] This letter does not address whether the Application satisfies any of the other criteria of Code § 432(e)(9).

Requirement that Suspension Be Reasonably Estimated to Avoid Insolvency

The regulations implementing Code § 432(e)(9) require that an applicant use actuarial projections to demonstrate that a suspension, in the aggregate, is reasonably estimated to achieve, but not materially exceed, the level that is necessary to avoid insolvency.[5] One of the projections required is a deterministic projection[6] of cash flow throughout an extended period under which the plan's available resources are projected forward using assumptions regarding the cash flows into the plan (e.g., contributions, withdrawal liability payments, and investment returns) and out of the plan (e.g., benefit payments and administrative expenses). The extended period over which an applicant must demonstrate that it satisfies the requirement to avoid insolvency is at least 30 years, starting with the first day of the plan year that includes the effective date of the suspension.[7]

Standards for Selecting Actuarial Assumptions Used in Projections

Treasury evaluated the assumptions and methods used in the Application based on the regulations. The regulations require that each of the actuarial assumptions and methods used for the required projections, as well as the combination of actuarial assumptions and methods, are reasonable, taking into account the experience of the plan and reasonable expectations.[8] In applying the regulations, Treasury referred to guidance provided by the professional standards that apply to the actuarial profession, which include the Actuarial Standards of Practice (ASOPs), as referenced in the regulations.[9]

The regulations require that, to be reasonable, each of the assumptions or methods must be appropriate for the purpose of the measurement, meaning, in this instance, that factors specific to a benefit suspension must be taken into account. The ASOPs also require that reasonable assumptions take into account historic and current demographic and economic data that are relevant as of the measurement date and that the assumptions have no significant optimistic or pessimistic bias. Further, the ASOPs provide that the plan's actuary must consider the materiality of the assumptions and the balance between the benefits of using more refined

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[4] Code § 432(e)(9)(D)(iv).
[5] 26 C.F.R. § 1.432(e)(9)-1(d)(5).
[6] A deterministic actuarial projection is a projection based on inputs that are assumed to occur. These projections are in contrast to stochastic actuarial projections, which estimate the probability of a range of outcomes as a result of random variation in one or more inputs (e.g., the investment return) over time.
[7] 26 C.F.R. § 1.432(e)(9)-1(d)(5)(ii)(C). The Application provides for a 32-year extended period, from April 1, 2020 through March 31, 2052.
[8] 26 C.F.R. § 1.432(e)(9)-1(d)(5)(iv)(B).
[9] TD 9765, 81 FR 25540, 25549. In this case, the relevant ASOPs are numbers 4, 27, 35, and 41.

actuarial assumptions (that is, assumptions that are based upon more extensive and specific study and research) and the cost of using those refinements.

Selection of Actuarial Assumptions for this Application

Treasury has concluded that two of the key actuarial assumptions used for the cash flow projections in the Application are not reasonable. Specifically, the mortality rate assumption and the assumption regarding the demographic characteristics of new entrants to the plan are not reasonable under the standards in the regulations. Because projections that rely on assumptions that are not reasonable were used in the Application, the Application fails to demonstrate that the proposed suspension is reasonably estimated to achieve, but not materially exceed, the level that is necessary to avoid insolvency. Accordingly, the proposed suspension does not meet the statutory requirements for approval because it does not satisfy the limitations set forth in Code § 432(e)(9)(D).[10]

The Mortality Assumption Is Not Reasonable

The mortality assumption used in the Application is not reasonable because it is based on a standard table that was used without adequate justification or a demonstration of the manner in which the table properly reflects the mortality experience of the Fund. Furthermore, when additional information was requested to support the use of the table, that information revealed that the Fund's actuary did not take into account relevant historic and current demographic data when selecting the standard table and that the standard table significantly overestimates the rate at which Fund participants and beneficiaries will die.

Mortality assumptions typically include both an assumption regarding the current mortality rate, which is reflected in a "base" mortality table, and an assumption about expected improvements in longevity, which are reflected in a mortality improvement scale. Standard mortality tables are developed using relevant historic experience and demographic data for standard populations, such as white collar workers in private pension plans.[11] Generally, the selection of a mortality table, including a standard mortality table, must be supported by appropriate experience from the plan, including actuarially credible evidence[12] demonstrating how the mortality experience used to develop the selected table is reflective of the mortality experience of the plan.

For the Application, an unadjusted standard base mortality table is used for current mortality rates, i.e., the RP-2014 Employee and Annuitant Mortality Tables (RP-2014 table), and that table

[10] MPRA Applications must be subject to public notice and comment pursuant to section Code § 432(e)(9)(G)(ii). If the Fund were to revise the cash flow projections in the Application (i.e., so that they are based on different, actuarial assumptions and methods), the Treasury Department could not rely upon those revised projections in the evaluation of the current Application because the revised projections would not have been subject to public notice and comment. *See Air Transport Ass'n of America v. FAA*, 169 F.3d 1 (D.C. Cir. 1999).
[11] The Society of Actuaries (SOA) published a series of mortality tables in 2014 reflecting the mortality experience for the population of participants covered under private retirement plans in the United States. The SOA is a professional organization in the United States engaged in actuarial research and education that publishes mortality tables and mortality improvement scales that may be used for private pension plans.
[12] This requirement, however, would not apply to very small plans, which would have no actuarially credible experience on their own.

reflects longevity using the Mortality Improvement Scale MP-2019 from the 2006 base year, projected forward generationally using Scale MP-2019.[13] However, the Application did not provide sufficient data and analysis to demonstrate how the mortality experience in the standard table was reflective of the Fund's mortality experience. Rather, for its rationale for the selection of the unadjusted RP-2014 table, the Application merely refers to a 2016 experience study prepared by the plan actuary that examines actual plan experience for plan years 2011 through 2015.[14] The Application states that in selecting the mortality assumption, "[n]o adjustments to the base mortality rates in RP-2014 were made because the [Actual to Expected] ratio in the 2016 experience study was 103%."[15]

When Treasury questioned why the RP-2014 table was selected without documenting a detailed justification, the Fund stated that it was not required to demonstrate the appropriateness of the use of the RP-2014 table since the use of that table is a safe harbor under Revenue Procedure 2017-43.[16] Treasury disagrees that Rev. Proc. 2017-43 provides a safe harbor for the use of the RP-2014 table. Rev. Proc. 2017-43 provides guidance on how to apply for a suspension and includes descriptions of the information required for a complete application. Section 6.03 of Rev. Proc. 2017-43 states that an application must include: (1) a description of each of the assumptions used in the projections, and (2) supporting evidence for the selection of those assumptions. Appendix B to Rev. Proc. 2017-43, which "may be used as a template" for providing the information required by Section 6.03, indicates that the mortality experience used in developing the total data set mortality rates in the RP-2014 Mortality Tables Report "may be treated as representative" of the expected mortality experience for the participants in the plan. However, this language merely describes the information that must be included in an application using the RP-2014 table—*after* an applicant has reasonably concluded (and provided the basis for its conclusion) that use of the RP-2014 mortality table is appropriate for the plan. That language is not intended to replace the regulatory requirement that the actuarial assumptions and a combination of those assumptions must be "reasonable, *taking into account the experience of the plan* and reasonable expectations" (emphasis added).[17]

It was not only the scant support for the mortality assumption included in the Application that caused Treasury to question the use of the RP-2014 table. In evaluating the minimal evidence the Application did provide to support the selection of the assumption, Treasury noted that that 2016 experience study was weighted on a "headcount" basis, rather than on an "amount weighted" basis, as the RP-2014 table is. The differences in weighting between the two tables skew the mortality results.[18] In the Fund's case in particular, the use of a headcount-weighted

[13] Application at pg. 315.
[14] Application pg. 322. The Application includes two 5-year experience study reports in Exhibit 6.04(2), beginning on pg. 340.
[15] Application pg. 322.
[16] 2017-31 I.R.B. 152.
[17] 26 C.F.R. § 1.432(e)(9)-1(d)(5)(iv)(B).
[18] Headcount-weighted tables measure mortality based on the number of deaths that occur over a period of time. In contrast, an amount-weighted table considers the number of deaths and the amount of benefits associated with those deaths over that same time period, such as whether participants with larger benefits will have greater longevity than retirees with smaller benefits; the mortality rates resulting from these amounts weighting are different than the rates based on the number of deaths alone. The use of amount-weighted rates is considered appropriate for the measurement of pension plan obligations in most cases; headcount-weighted rates are typically used in more limited

study is inappropriate because of the Fund's non-homogenous population and benefit structures, which result in a wide range of benefit amounts for participants.[19] The Fund's cash flows are heavily weighted toward participants with larger benefits; thus, amount-weighting exposures are essential for determining the Fund's mortality experience in relation to the RP-2014 table.

Given that the Application did not provide a detailed rationale for use of the RP-2014 table and that the 2016 experience study was problematic because it was headcount-weighted, Treasury requested additional amount-weighted information to support the reasonableness of the Fund's mortality assumption. Specifically, the Fund was asked to provide information and analysis to support the conclusion that the Fund's amount-weighted experience analysis (based on the most recent 3-5 years of experience) is fully or partially credible and provides support for use of the RP-2014 mortality table.[20]

The Fund subsequently submitted an amount-weighted experience analysis (for ages 50 and older) by year and in aggregate, for the 2014-2018 plan years, as well as the calculation of the plan's credibility factor (separate for males and females).[21] However, this information exposed another issue with the mortality assumption used in the Application by showing that it assumes higher mortality rates than are supported by the amount-weighted experience during recent years. Specifically, if future experience is similar to the recent experience (determined by the plan actuary on an amount-weighted basis), but considering the partial credibility of the Fund's experience, the Fund is expected to have 15% fewer deaths for the male population over the extended period, which is a significant deviation given that the Fund's population is predominantly male.[22] In addition, the year-by-year amount-weighted experience analysis indicates that the difference between the Fund's assumption and the Fund's actual experience has been cumulatively widening.

In sum, the Fund's use of the unadjusted RP-2014 standard table is not reasonable. The Application itself provided only limited support for the choice of this mortality assumption. In addition, the Fund's use of headcount-weighted experience is not reasonable to support the use of that assumption. Further, because the mortality rate assumption used in the Application was

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circumstances in which benefits are similar in amount for all plan participants, such as for retiree health benefits. *See*, Society of Actuaries, "RP-2014 Mortality Tables Report," revised November 2014, section 13.5, pg. 52. Available at https://www.soa.org/globalassets/assets/Files/Research/Exp-Study/research-2014-rp-comment.pdf (last visited August 2, 2020). *See also*, Selecting and Documenting Mortality Assumptions for Pensions, Q&A 27. Available at https://www.actuary.org/sites/default/files/files/Mortality_PN_060515_0.pdf.

[19] Based on the census data provided by the Fund as of April 1, 2019, post suspension, 50% of participants in pay status would receive less than $313 per month; 40% would have a monthly benefit between $313 and $2,217; 5% would have a monthly benefit between $2,218 and $3,588; and the remaining 5% would have monthly benefits ranging from $3,589 to over $25,000.

[20] The Fund initially indicated that an amount-weighted experience study was not appropriate because the Fund's mortality experience is not credible. In response, Treasury suggested that, because the Fund's mortality experience appeared to be partially credible, the Fund could utilize the methodology prescribed by Rev. Proc. 2017-55 to develop a partial credibility weighting factor for the Fund's mortality experience. Rev. Proc. 2017-55 sets out generic procedures for single-employer plans with partial credibility to apply to the Internal Revenue Service for approval to use plan-specific substitute mortality tables for funding purposes. *See* 2017-43 I.R.B. 373.

[21] This analysis was developed by the plan actuary based on standards set forth in Rev. Proc. 2017-55.

[22] About 70% of plan participants are male, based on census data provided by the Fund. The projections show a 5% negative differential for the Fund's female population.

not consistent with historic and demographic experience relevant as of the measurement; Treasury has concluded that it is not reasonable. Therefore, the proposed suspension does not satisfy the statutory requirement that it be reasonably estimated to avoid insolvency.

The New Entrant Assumption Is Not Reasonable

To project cash flows, an applicant must make an assumption regarding the demographic characteristics of plan participants, including the characteristics of employees who replace terminating and retiring workers or otherwise become active participants (i.e., future new entrants to the plan). In particular, a new entrant assumption must project the "entry age"—the assumed age at which new participants enter (or return to active status in) the plan.[23] Further, as for any actuarial assumption, to be appropriate for the purpose of the measurement, the new entrant assumption must be selected in a manner that takes into account factors specific to the measurement.

The anticipated pattern and magnitude of change in the level of Fund assets is sensitive to assumptions (like the age at which new active participants are hired or rehired) that affect the amount and timing of anticipated benefit payments. Accordingly, the new entrant assumption for purposes of these cash flow projections must be developed in a refined manner that reflects expected cash flows.

The new entrant assumption used in the Application fails to take into account the prevalence of rehires, even though it is clear from recent actuarial valuations that a significant portion of the new entrants each year are terminated vested participants who are rehired. For example, in each of the last three valuation reports, about 30% of the new entrants were formerly terminated vested participants.[24]

The Application's new entrant assumption is not reasonable because it does not take into account relevant historic and current demographic data (that is, data available regarding demographic characteristics of recent rehires) and it has a significant bias in that it underestimates the average entry age of new active participants, resulting in a significant understatement of benefit payments from the Fund. Specifically, it is not appropriate for the Fund to utilize a new entrant assumption that excludes recently rehired participants if doing so produces materially different results than use of a refined assumption.

The new entrant demographic profile used in the Application was developed based only on the demographic characteristics of the new hires who had not previously participated in the Fund and did not consider the characteristics of rehires from terminated vested status. Based on the experience analysis provided by the Fund, the demographic characteristics of new entrants are quite different if the rehired participants are included in the analysis. Treasury has estimated that the average entry age of new entrants when considering the demographic characteristics of rehires is 5 years older than the average entry age if rehires are excluded from the analysis.

[23] The new entrant assumption also includes assumptions about the new participants' gender, pay, and contributions.
[24] The 2017 Actuarial Valuation Report (AVR) shows 32% (1,155 of 3,605) of new entrants are rehires (Application, p. 1450). The 2018 AVR shows 29% (1,023 of 3,580) of new entrants are rehires (Application, p. 1492). The 2019 AVR shows 30% (1,068 of 3,615) of new entrants are rehires (p. 28 of the April 1, 2019 actuarial valuation report published in February 2020).

The inclusion of the demographic characteristics of the rehired participants would have a significant impact on the Fund's projections. The cumulative benefit payments through the extended period for new entrants would be almost 70% higher ($63M) than shown in the Application, and the projected market value of assets at the end of the extended period would be more than 10% lower ($135M) than the projected market value shown in the Application.

Relevant historic and current demographic data, such as data on the actual entry ages of all new entrants to the Fund over any relevant period, should have been reviewed and taken into account in the selection of the new entrant demographic profile. It is the view of Treasury that the new entrant assumption used in the application is not supported by the Fund's experience for new entrants including rehired participants and that the assumption is not reasonable.

CONCLUSION

For the reasons set forth above, Treasury has concluded that the Application fails to demonstrate that the proposed suspension satisfies the requirement that it be reasonably estimated to achieve, but not materially exceed, the level that is necessary for the Fund to avoid insolvency. As a result, the Application fails to demonstrate that the proposed suspension satisfies the limitations set forth in Code § 432(e)(9)(D), which is required for approval of a proposed suspension. Accordingly, the Application is denied.

This notification letter will be made public in order to inform plan participants and beneficiaries of the outcome of Treasury's review.

Respectfully,

Danielle Norris

Danielle Norris

MPRA Director