

Response to *The Washington Examiner* Editorial on “Worst-Funded Union Pension Plans”

On July 9, 2010, *The Washington Examiner* published an editorial by Mark Tapscott titled “Are you depending on one of these 108 worst-funded union pension plans?” Over the past several weeks, this editorial has gained some attention, and some parties have even distributed it to people covered under these pension plans.

It is true that many pension plans – both union and non-union – are facing challenges in the wake of the financial market collapse of 2008 and continuing poor economic conditions. However, *The Examiner* editorial uses misleading information to portray union pension plans as being worse funded than they actually are.

Misleading Funded Percentages in *The Examiner*

The “funded percentage” for a pension plan is the ratio of the value of its assets to the value of its liabilities. There are several issues with the funded percentages presented in *The Examiner* editorial, which were originally presented in a report by Moody’s from September, 2009. The main issues are as follows:

- *The Examiner’s* funded percentages are based on out-of-date information. In most cases, the information used was two or three years old at the time the editorial was written.
- *The Examiner’s* funded percentages were measured at an extreme low point in the financial markets. They reflect an estimate of the colossal investment losses in 2008, but they ignore the generally positive returns in 2009.
- *The Examiner’s* funded percentages were determined using assumptions and methods that are much more conservative than what is required under federal law or what is used to actually fund these plans.

These factors combine to understate the funded percentages for these union plans by an average of 20% to 25%, relative to their actual current position.

For example, one particular plan was cited in the editorial as being below 70% funded; it is actually 90% funded as of the beginning of its current plan year. Another plan was cited as being below 60% funded; it is actually 84% funded as of the beginning of its current plan year.

Where to Get Better Information

For decades, the boards of trustees of multiemployer pension plans have been working to ensure that the benefits promised to participants and beneficiaries will be secure in the future. While the market collapse of 2008 and current economic conditions make that endeavor more challenging, the trustees are still striving to sustain the plans for the generations to come.

If you are a participant or beneficiary under a multiemployer pension plan, the plan will automatically send you annual notices reporting its funded status, as required by federal law. You can also contact the plan itself to get additional information. The information you get directly from your plan will be much more up-to-date, accurate, and reliable than what was presented in *The Examiner*.

Technical Issues with Moody's Approach

As noted earlier in this bulletin, the funded percentages shown in *The Examiner* editorial were taken from a Moody's report published in September, 2009. The Moody's report attempted to use publicly-available information to estimate the funded percentages of multiemployer pension plans as of the end of 2008. The following is a list of technical problems with the Moody's approach that result in a very misleading picture painted by *The Examiner*.

- Out of date information – The Moody's report compiled information that was publicly available in 2009. In general, this information consisted of government filings from 2007, with plan liabilities being reported as of the beginning of the year and asset values being reported as of the end of the year. That means, by the time *The Examiner* editorial was written in 2010, asset values were over two years old, and plan liabilities were over three years old.
- Measurement at an historic low point – In general, the Moody's report relied on asset values that were as of the end of 2007. Moody's then made a rough attempt to roll forward the asset values to the end of 2008 to reflect the historic investment losses incurred during that year. However, the Moody's estimates do not attempt to estimate experience during 2009, which was a positive investment year for most multiemployer pension plans. To reflect 2008 losses but exclude 2009 gains will in most cases understate a plan's true funded percentage as of 2010.
- Approximation of 2008 losses – In rolling forward plan asset values from the end of 2007 to the end of 2008, Moody's made some very simplified assumptions. First, Moody's assumed that all plans are invested in an asset mix of 65% stocks, 35% bonds, and 10% other assets. Then, it assumed that in 2008, all stocks returned -38.5%, all bonds returned 1.0%, and all other assets returned -30.0%. This results in a weighted average investment return of -27.8% for 2008 for every pension plan. In actuality, investment returns for the calendar year 2008 ranged from -20% to -30% for most plans, depending on the specific investments they held. Needless to say, the simplified approach could produce results that are very different from reality. (The simplified approach also ignores the fact that some plans may not be based on the calendar year.)
- Incorrect liabilities used – Under federal law (specifically, the Pension Protection Act of 2006, or "PPA"), the funded status for a multiemployer plan is determined based on the plan's "actuarial accrued liability." This liability measure reflects the plan actuary's best estimate of future returns on plan assets, based on the plan's actual investment allocation. The Moody's approach uses the plan's "current liability" instead. Current liability is based on very conservative assumptions, in particular, that the plan is invested entirely in corporate bonds. The end result is that the Moody's approach may overstate plan liabilities by 5% or more versus what is required under PPA.
- No asset smoothing used – Under PPA, the funded percentage required to be reported for a multiemployer plan is based on the plan's "actuarial value of assets." The actuarial value of assets usually reflects smoothing of prior year investment return volatility, allowing plan Trustees to appropriately react (and not overreact) to investment gains and losses year after year. The Moody's approach simply uses an estimate of the plan's "market value of assets," which does not reflect any smoothing. In most cases, the Moody's approach understates plan asset values by 20% versus what is required under PPA.

As demonstrated above, there are numerous issues with the approach used by Moody's in its September, 2009 report for determining the funded percentages for multiemployer plans. To present these funded percentages in 2010 – as was done by *The Examiner* – is at best incorrect, and at worst, intentionally misleading.

If you are a participant in a multiemployer pension plan and you have questions regarding its funded status, you should contact the plan itself to receive better information.

Horizon Actuarial Services, LLC does not practice law, nor do we provide tax advice. Please consult with your legal counsel or tax advisor for information specific to your plan's legal or tax implications.

Horizon Actuarial Services, LLC is an independent consulting firm specializing in providing actuarial and consulting services to multiemployer benefit plans. For more information on our company or to contact us for additional information, please visit our website at www.horizonactuarial.com.