Milliman analysis shows multiemployer pension funded status falters in 2018

Despite setbacks most plans have improved since 2008, but more help may be needed for the rest

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Milliman's Spring 2019 Multiemployer Pension Funding Study reports on the estimated funded status of all U.S. multiemployer plans as of December 31, 2018.

Key findings

- The estimated investment return for our simplified portfolio for the 12 months ending December 31, 2018, was about -5%, resulting in double-digit losses compared to plans' investment return assumptions.
- The average investment return assumption dropped from 7.34% in our Fall 2018 study to 7.26%.
- The aggregate funded percentage for multiemployer plans is estimated to be 74% as of December 31, 2018, down from 81% as of June 30, 2018.
- Many critical and declining plans will not be able to avoid insolvency without additional tools or options.
- Since 2008, the majority of plans are trending toward stronger financial health despite investment setbacks.

Current funded percentage

Figure 1 shows that, for the six-month period ending December 31, 2018, the overall funding shortfall increased by $51 billion to a total shortfall of $176 billion. The aggregate funded percentage dropped from 81% to 74%.

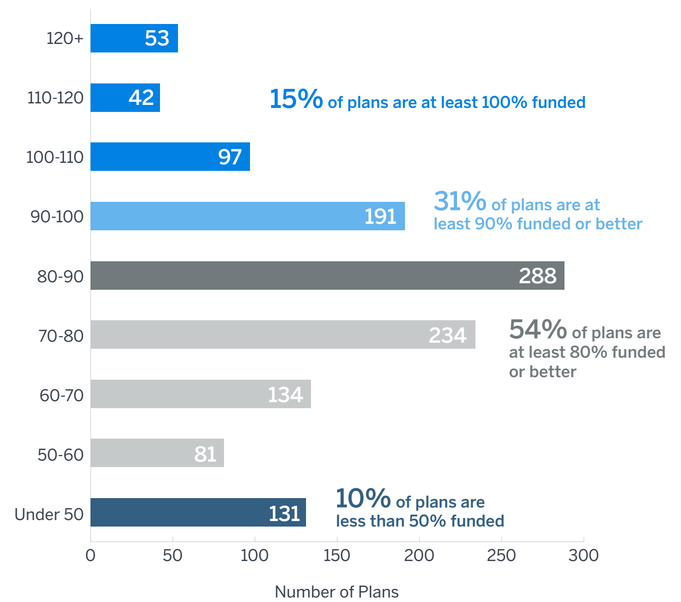
FIGURE 1: AGGREGATE FUNDED PERCENTAGE (IN $ BILLIONS)

	6/30/2018	12/31/2018	Change
Accrued benefit liability	$666	$678	$12
Market value of assets	541	502	(39)
Shortfall	$125	$176	$51
Funded percentage	81%	74%	(7%)

Based on plans with complete IRS Form 5500 filings. Includes 1,256 plans as of June 30, 2018, and 1,251 plans as of December 31, 2018.

Figure 2 is a distribution of funded percentages for all plans in the study as of December 31, 2018.

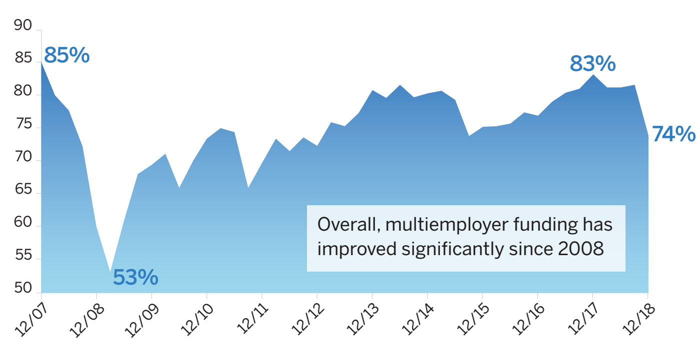
FIGURE 2: MARKET VALUE FUNDED PERCENTAGE (%)



Historical funded percentage

Figure 3 provides a historical perspective on the aggregate funded percentage on a market value basis of all multiemployer plans since the end of 2007.

FIGURE 3: AGGREGATE HISTORICAL FUNDED PERCENTAGE MARKET VALUE BASIS



While the ride toward improved financial health has been rocky, overall multiemployer funding has improved significantly since 2008. The aggregate funded percentage as of December 31, 2018, was 74%, a step back from December 31, 2017. The decline in 2018 was primarily driven by poor asset returns. We estimate that average returns for 2018 were approximately -5%. With assumed investment returns generally between 6% and 8%, asset losses ranged from 11% to 13% below expectations.

Discount rates

The funded percentages shown in Figures 1 to 3 reflect liabilities measured using each plan's assumed discount rate (typically the assumed investment return on plan assets). Assumed discount rates are generally between 6% and 8%, with a weighted average assumption of 7.26%, compared to 7.34% in our prior study. The reduction was primarily driven by the Central States, Southeast and Southwest Areas Pension Plan, which lowered its assumption from 6.25% to 5.50%.

It is not uncommon to see critical and declining plans utilizing a lower investment return assumption than other plans, because they are projected to go insolvent within the next 20 years (many plans much sooner than that, such as Central States). Short-term capital market assumptions from most financial experts predict markedly lower returns in the near future than what might be expected for longer time horizons. Thus, some critical and declining plans have set their assumptions accordingly, putting less weight on long-term expectations.

In contrast, most financial experts anticipate that, over a longer time horizon, capital markets will more closely resemble historical norms, resulting in higher expected returns over those longer periods. Plans expected to remain solvent beyond 20 years may assign more significance to longer-term outlooks, which generally results in higher investment return assumptions.

One of the items considered during 2018 by the Joint Select Committee (JSC) on the Solvency of Multiemployer Pension Plans was a cap on the discount rate for multiemployer pension plans, as we alluded to in a recent Multiemployer Alert. We estimate this cap would have been in the neighborhood of 6% as of December 31, 2018.

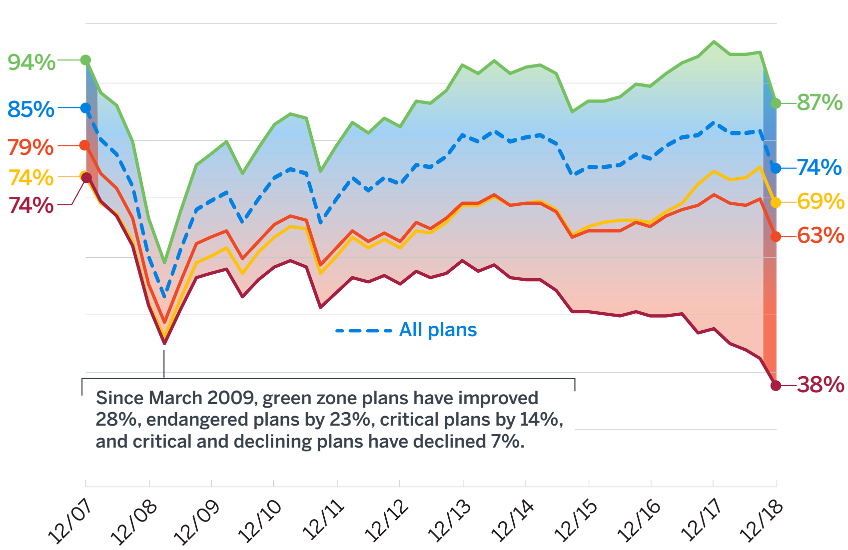
To provide an idea of the impact of such a cap, if the liabilities for all multiemployer plans in Figure 1 were recalculated using assumed discount rates no higher than 6%, then the resulting aggregate liability would be approximately $800 billion. When compared to the total market value of assets of $502 billion, the result would be an aggregate funded percentage for all multiemployer plans of approximately 63%, as compared to the current reported figure of 74%.

While the JSC was unable to provide any legislative solutions during 2018, discussions have continued at the committee level during 2019. Bills related to low-interest long-term loans for financially distressed plans have been reintroduced in the House and Senate. All stakeholders should continue to monitor the issues and be prepared to act upon any developments that unfold.

Funding history by zone status

Figure 4 shows the historical funded percentage of all multiemployer plans since the end of 2007 by their current zone status. For example, the green line shows the historical funded percentages of plans currently in the green zone without regard to their previous zone statuses. The blue dotted line represents all plans combined.

FIGURE 4: AGGREGATE HISTORICAL FUNDED PERCENTAGE BY CURRENT ZONE STATUS



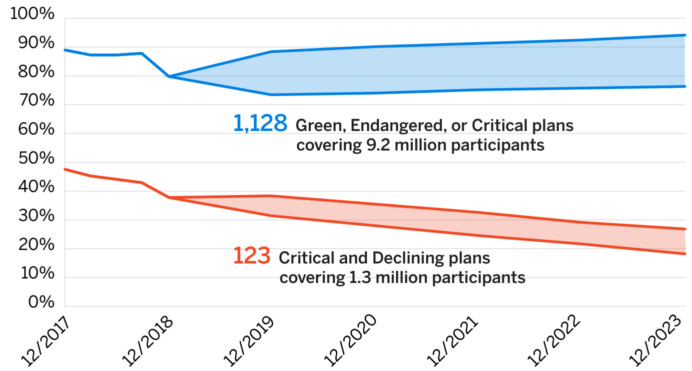
ZONE STATUS	NUMBER OF PLANS	NUMBER OF PARTICIPANTS
Green	783	6.0M
Endangered	135	1.0M
Critical	210	2.2M
Critical and Declining	123	1.3M
All Plans	1,251	10.5M

While market losses in 2018 hampered improvement, the aggregate funding level for all plans other than critical and declining plans has improved since 2008. These 1,128 plans represent 90% of all multiemployer plans and cover 88% of all participants (9.2 million). They have benefited from generally strong asset returns, and in some cases have been able to adjust benefits, contributions, or both in order to make progress toward restoring fund health. Because critical and declining plans generally have heavier negative cash flows, they need more significant and sustained investment gains to recover.

What lies ahead?

Figure 5 illustrates the impact one year's investment return can have on the projected funded status over the next several years. Plans that are in critical and declining status now are shown in red and all other plans are shown in blue. The solid lines illustrate the impact on the projected funded percentage if actual returns for 2019 differ from the assumed return by plus or minus 10%, followed by the assumed return for each year thereafter.

FIGURE 5: PROJECTED FUNDED PERCENTAGE THROUGH 2023 CRITICAL AND DECLINING PLANS VERSUS ALL OTHER PLANS



While the primary driver of financial health of multiemployer pension plans continues to be asset performance, more tools are needed for many critical and declining plans to recover. As Figure 5 illustrates, even a significant bounce back from 2018 cannot right the ship for critical and declining plans. Many of these plans are likely headed for insolvency absent Congressional action. In contrast, in the aggregate, non-critical and declining plans can withstand another modest investment loss in 2019 and remain on a path to recovery.

ABOUT THIS STUDY

The results in this study were derived from publicly available Internal Revenue Service (IRS) Form 5500 data as of February 2019 for all multiemployer plans, numbering between 1,200 and 1,300, depending on the measurement date used. Data for a limited number of plans that clearly appeared to be erroneous was modified to ensure the results were reasonable and a sufficiently complete representation of the multiemployer universe.

Liability amounts were based on unit credit accrued liabilities reported on Schedule MB, and were adjusted to the relevant measurement dates using standard actuarial approximation techniques. For this purpose, each plan's monthly cash flow, benefit cost, and actuarial assumptions were assumed to be constant throughout the year and in the future. Projections of asset values to the measurement date reflect the use of constant cash flows and monthly index returns for a simplified portfolio composed of 45% U.S. equities, 20% international equities, and 35% U.S. fixed income investments.

Significant changes to the data and assumptions could lead to much different results for individual plans, but would likely not have a significant impact on the aggregate results or the conclusions in this study.

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