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Some unions turning to variable benefit pension plan model

By: [Hazel Bradford](#)

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Jeanette Cooper doesn't believe there can be one single template for variable benefit plans.

As a special committee in Congress continues to grapple with ideas to help struggling multiemployer pension funds and to keep others from the same fate, an increasing number of trustees are forging ahead with shared-risk or variable benefit plan designs that can better match benefits to market returns.

"If Congress does something creative with pension reform, that's great, but we weren't going to wait around for it. We wanted to take the initiative just in case something isn't worked out," said Jason Engels, chairman of the \$95 million New Orleans Carpenters Pension Plan, a plan close to 100% funded that added a variable plan design for all benefits that have accrued since May.

The basic premise of a variable defined benefit or annuity pension plan is that benefits are adjusted up or

down based on investment returns. The assumed rate of return is called the hurdle rate, typically between 4% and 6%, which determines whether benefits for all participants, including retirees, rise or fall on a plan year basis.

Like current practice, trustees set benefit accrual rates, including one-time increases, and bargaining parties negotiate contribution rates. However, annual adjustments to the variable benefit reflecting the plan's investment performance are driven by a preset formula.

"No one variable plan design works for all plans. The main objectives of a pension board will influence the ultimate design, including balancing contribution risk and benefit risk resulting from investment volatility," said Jeanette Cooper, vice president and consulting actuary with Segal Consulting in Atlanta. She worked with the carpenters' plan, which features a 2.5% of salary accrual rate, a 5% investment return hurdle rate and a maximum 10% adjustment — up or down — in any year. The investment return is based on a five-year average of market returns, and benefits continue to float when participants are in retirement.

"We've been thinking about it for several years. It seemed like a good opportunity to go ahead and add the variable annuity design to guard against volatile markets and offer a plan attractive to our members as well as current and future employers," said Mr. Engels. Other pension funds in the five states covered by the Central South Carpenters Regional Council where he is executive secretary-treasurer are also considering it, as plan trustees become more open-minded and plan participants realize the increasing demands on multiemployer defined benefit plans. "Things are changing, and they are going to have to change," he said, noting most plan participants viewed the new design favorably. "Change is hard, of course, but our members understand the importance of maintaining a well-funded plan.

"With this plan design, our contractors and members both share, good or bad. I tell them it's better to put a plan in place now that accounts for potential future market downturns than be reactionary 20 or 30 years down the road with unanticipated benefit cuts or contribution increases. We are just putting the proper measure in place to make sure this plan stays well-funded," Mr. Engels said.

Other features

Features of other variable plans in place or on the drawing board depend on recommendations from the actuarial firms and consultants who are spending increasing amounts of time fielding calls of interest, modeling the concept for their multiemployer plan clients, and launching them.

Some have floors on how low benefits can dip if markets drop, and some build reserves to offset benefit drops in those cases. One approach is to add variable features to existing plans so that benefits change going forward, while other trustees choose to start a variable plan and manage it along with the existing legacy defined benefit plan.

Launching a variable plan alongside a legacy defined benefit plan does not address withdrawal liability in the legacy plan but does diminish the likelihood of withdrawal liability in the new plan. For the carpenters' plan, "using a variable benefit for new accruals reduces the likelihood of having withdrawal liability as more and more of the total benefits become variable," Ms. Cooper of Segal said.

Gene Kalwarski, CEO of actuarial consultant Cheiron Inc. in McLean, Va., said variable plan design options "all over the place" are being presented to more plans. "We alone are discussing it with a couple dozen situations. Multiply that by five for the other firms," he said.

Some potential adopters came to the idea after considering switching to a defined contribution plan to calm contributing employers' concerns over mounting contributions or unfunded liabilities, while others even made the switch to defined contribution, before realizing the variable plan option. "The barbells are DB and DC, and people haven't spent enough time in the middle," said Mr. Kalwarski.

Trustees for the United Food and Commercial Workers Union Local 663 in Minneapolis started discussing a variable benefit plan in addition to their \$550 million defined benefit plan about five years ago, and began seriously studying it about two years ago, said Robert Kurak, a vice president and consulting actuary with Segal Consulting in Minneapolis. The variable plan will take its first contributions in January and cover 4,000 active participants. "There was a lot of interest on both sides of the table in securing lifetime benefits, where they don't have to worry about benefits becoming underfunded," he said.

More expected to switch

Kelly Coffing, a principal and consulting actuary with Milliman Inc. in Seattle, expects to see "more and more" variable plans in the multiemployer realm. By January, her firm will have converted 10 multiemployer plans and two corporate plans to its trademarked "sustainable income" variable design. The first plan went live in 2015. It calls for no floor on how low benefits can dip, but it sequesters some investment earnings from high-return years to build up a reserve that can be used to protect future benefits.

"I think we are really at an inflection point where variable plans could be the future of DB plans," said David Blitzstein, a former UFCW benefits director and longtime advocate of variable plan design who consulted on the Minneapolis plan. While the concept has been around for a while, two major financial downturns in less than two decades helped actuaries, plan consultants and multiemployer plan trustees rediscover it, he said.

"I think people are frustrated with investment risk and they are frustrated with changes in demographics," said Mr. Blitzstein, who is now president of Blitzstein Consulting LLC advising labor unions and multiemployer plans. "I like the potential for what it can do. You can derisk your portfolio and you can keep your promises to participants."

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