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An Update From Bodman PLC

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Sixth Circuit Addresses Actuarial Assumptions Regarding Withdrawal Liability

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In *Sofco Erectors, Inc. v. Trustees of the Ohio Operating Engineers Pension Fund ("Sofco")* (September, 28, 2021), the Sixth Circuit Court of Appeals issued a long awaited decision regarding the appropriateness of interest rate assumptions used by union pension funds to calculate withdrawal liability. The Court affirmed a district court's opinion holding that the Ohio Operating Engineers Pension Fund's ("Fund") use of the "Segal Blend" violated ERISA.

Background

When multiemployer pension plans have unfunded "future liabilities," employers who cease to have an obligation to contribute to a plan are assessed a portion of the unfunded liability ("withdrawal liability"). Under ERISA, a plan must use reasonable actuarial assumptions in calculating withdrawal liability. Two important assumptions are: 1) what rate is appropriate to determine the minimum funding necessary to pay future liabilities; and 2) what rate is appropriate to discount the future liabilities to present value. The use of a low discount rate in either situation can greatly increase the withdrawal liability assessment to the withdrawing employer.

The Court's Decision

In *Sofco*, the Fund's best estimate of the rate of return on current assets for minimum funding purposes was 7.25%. Although it used the 7.25% rate to determine the minimum funding, the Fund used a "Segal Blend" rate (blending the Pension Benefit Guarantee Corporation rate of 2-3% with the Fund's best estimate of the rate of return – in this case 7.25%) to discount the future liabilities to present value and, ultimately, determine the withdrawal liability. The Court held that the Fund's use of the Segal Blend to discount future liabilities while simultaneously using the 7.25% rate of return on current assets to ensure minimum funding violated ERISA because the discount rate was not the actuary's best estimate of anticipated experience under the plan. The Court further stated that in this case the use of the Segal Blend to assess withdrawal liability is unreasonable because it incorporates "an interest rate used for plans that essentially go out of business, even though [this Plan is] neither going out of business nor required to purchase annuities to cover the departing employer's share of vested benefits."

Takeaways for Employers

Employers who are facing withdrawal liability should scrutinize the actuarial assumptions used by the pension fund and consider whether they have a basis for challenging those assumptions as unreasonable. A successful challenge could greatly reduce the employer's withdrawal liability.

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