



Recent Union Negotiations

Strategies & Results

Over the course of 2008, our pension actuaries and retirement consultants have been busy assisting our clients with various union negotiations. While you may not have union employees, we think you will still find these case studies helpful. Each case study demonstrates the methods employers have used to balance the need to control costs, while offering solutions for all employees. They also illustrate ways employers have been able to transition to either a Cash Balance arrangement or a Defined Contribution (“DC”) focused plan without completely abandoning their Defined Benefit (“DB”) plans.

If your organization is looking at a change in the delivery of your retirement benefits, our experience and past successes can serve as a foundation to help you find the right plan for your budget and your employees.

Case #1

One of our for-profit clients maintained a traditional final pay DB plan and a matching 401(k) plan. In a decision to stabilize and control costs, they asked us to study a transition to a fully DC program or to adopt a cash balance plan in lieu of the traditional DB plan. They decided upon a “soft freeze” of the existing DB plan and to adopt a cash balance plan for new employees. Continuing the DB plan in a cash balance design would allow them to offer employees an individual account program, with service-based pay credits and a guaranteed interest credit, while effectively utilizing their accumulated accounting gains within a professionally guided investment structure.

Their plan covered employees of three unions. The use of the new cash balance plan to cover these union employees needed to be negotiated under the next collective bargaining agreement opening at the end of 2007. In the spring of 2007, the employer “pre-negotiated” with the unions, familiarizing them with the desire for the plan change and the motivations for the change. The union representatives were aware of another employer in the state that had negotiated a similar change to a cash balance plan. The United Auto Workers (“UAW”) had recently announced cash balance plans to cover new hires at GM and Chrysler. They gave a nod to the principle of the new plan design.

When the formal negotiations opened in the fall of last year, the employer proposed a plan with service-based pay credits progressing from 5% to 9% after 15 years of service. During the negotiations, many ideas were considered:

- Higher pay credits
- Alternative interest credit rates
- Including existing non-vested employees
- Improvements in the closed DB plan, including extending the benefit accrual past 30 years of service, reducing early retirement reduction factors, and a cost of living adjustment for existing retirees
- Improving the 401(k) plan match
- Improving the subsidy upon early retirement under the post-retirement medical plan

Client U·P·D·A·T·E

The Result: The negotiations were completed with an agreement on retirement benefits as follows:

- Adopt a cash balance plan for new employees with service-based pay credits from 5% to 11% after 20 years, interest credits of 30 yr T-bills, and three-year graded vesting.
- Amend the traditional DB plan to provide unreduced early retirement benefits on a rule of 85 instead of 90, and lump-sum pre-retirement death benefits.
- Amend the 401(k) plan to provide for loans.

Case #2

A not-for-profit client requested our assistance in advising them regarding pension plan design options for their upcoming negotiations. The benefit formula, pre-negotiation, was 1.6% x Final Average Pay (“FAP”). Management was initially seeking a “hard freeze” to rein in projected contributions and FAS 87 expense. They sought to replace DB plan benefits for all current and future participants with a 2% to 6% service-weighted DC plan matching contribution (matching 50% of the participant’s voluntary contribution, up to 4% to 12%).

The union did not want benefits frozen and threatened to strike. We worked with the client on several plan design options that were offered to the union. These included an innovative approach whereby benefits would be frozen temporarily for three years for current DB participants with a 1.35% x FAP formula after the temporary freeze, and new participants would receive the 2% to 6% service-weighted DC matching contributions described above. The freeze would serve to give management the breathing room they needed to reduce funding and expense costs considerably over the next three years, and also give them the opportunity to budget for contributions required after the end of the three year freeze.

The Union stood firmly and said they would not agree to either the three-year freeze or new participants participating in a DC plan. The contract expired and the Union presented the client with a strike notice, and went on strike for four weeks. Negotiations continued for two weeks after the strike, and then stopped completely for 12 days. After both sides came back to the table, they quickly worked out an agreement that included a two year temporary freeze for current DB participants, with new participants receiving the 2% to 6% matching contribution.

The Result: The temporary benefit freeze met managements’ objectives of controlling relatively high short-term funding and expense requirements, as well as the Union’s objective of maintaining DB plan benefits for its members.

Case #3

We recently assisted a not-for-profit client with a difficult negotiation issue involving reducing retirement costs. The client had a traditional DB plan designed decades ago that was rapidly becoming prohibitively expensive. While reasonably well funded, the ongoing normal costs under the Pension Protection Act (“PPA”) were projected at 10% of payroll increasing to 14% over a 15-year period. The benefit provided was 60% of final average pay, with a small offset that was originally intended to represent one half of Social Security benefits, but had not been indexed for many years. In addition, the benefit was earned pro-rata over a participant’s career, but the full 60% could be earned in as little as 15 years (i.e., hired at age 50). Someone hired at age 50 would earn the same pension at age 65 as someone hired at age 21 (assuming equal final average earnings at retirement).

Our client’s goals were to reduce costs, while protecting those closest to retirement, and gradually transitioning to a DC arrangement. The initial structure of the proposals was as follows:

- Participants over age 60, or whose age plus service (points) were over a certain threshold, would retain the current program.
- Participants with fewer points would get a reduced DB formula, plus a matching contribution in the 403(b) plan.
- Participants under a certain point threshold would have the DB benefit “frozen” (only increases in final average pay would increase the benefit), a core DC plan contribution, and also have a matching contribution in the 403(b) plan.
- New participants would get a core DC plan contribution and a match.

The Union acknowledged that the current program was costly and inequitable. However, they strongly objected to the emphasis on DC programs. They felt that not enough employees would participate to receive the match. They also felt that with turbulent capital markets, employees would not invest well enough to achieve adequate retirement monies.

The Result: The contract expired and the union presented our client with a strike notice. They went back to the table and hammered out a compromise that put less emphasis on matching contributions, replaced some of the DC plan features with a cash balance feature within the DB plan, and provided a guaranteed rate of return on the cash balance accounts. The client was still able to significantly reduce future costs, and the Union achieved the retention of more DB features via the cash balance arrangement.

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