Practical Guide for Dealing with Employee Benefits Issues in Challenging Economic Times: PBGC, Underfunded Defined Benefit Plans, and Distressed Companies

20th Annual Spring Symposia
ABA Section of Real Property, Trust & Estate Law
April 30, 2009 ● Washington, DC

Harold J. Ashner
Keightley & Ashner LLP

KEIGHTLEY & ASHNER LLP
The PBGC-Focused Law Firm

Overview

- A Brief Introduction to PBGC
- Defined Benefit Plan Funding—Challenges and Options
- PBGC's Pursuit of "Downsizing Liability"
- "Early Warning Program" Negotiations
- Distress Terminations
- PBGC-Initiated Terminations
- Bankruptcy Claims and Disputes

A Brief Introduction to PBGC

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- PBGC structure/governance/oversight
  - Government corporation
  - Board of Directors: Cabinet-Level Secretaries
    - Labor (Chair of Board)
    - Treasury
    - Commerce
  - Day-to-day: Run by Director (Senate-confirmed)
  - Political oversight (Congressional Committees)
    - Senate Finance Committee
    - Senate Health, Education, Labor & Pensions Committee
    - House Ways/Means Committee
    - House Education/Workforce Committee

A Brief Introduction to PBGC (Cont.)

- PBGC funding
  - No "full faith and credit"
  - No tax dollars
  - Funded by:
    - Premiums paid by employers/plans
    - Assets in PBGC-trusteed plans
    - Recoveries from employers
    - Investment returns

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A Brief Introduction to PBGC (Cont.)

- Termination of PBGC-covered plans
  - Title IV of ERISA allows only:
    - Standard termination (fully-funded)
    - Distress termination (underfunded)
    - Involuntary (PBGC-initiated) termination (underfunded)
  - Underfunded termination consequences—participants
    - *Will* receive guaranteed benefits
    - *May* receive some/all non-guaranteed benefits
    - Most participants' benefits are fully guaranteed
    - For many participants, key loss is lump sum option

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A Brief Introduction to PBGC (Cont.)

- Termination of PBGC-covered plans (cont.)
  - Underfunded termination consequences—employer
    - Employer liability for underfunding for *all* benefits (guaranteed and non-guaranteed)
    - Calculated using conservative PBGC assumptions (insurance industry annuity pricing)
    - Unique liability rule: *Each* member of sponsor's controlled group jointly and severally liable for *full* amount of:
      - Employer liability
      - Unpaid contributions
      - Unpaid premiums and new "termination premium" ($1,250 per participant, per year, for 3 years)

A Brief Introduction to PBGC (Cont.)

- Termination of PBGC-covered plans (cont.)
  - Underfunded termination consequences—PBGC
    - Becomes successor trustee of plan
    - Pays guaranteed and (generally) some non-guaranteed benefits
    - Typically incurs loss based on underfunding and collects little/nothing on claims against employer
    - PBGC may be able to protect itself before bankruptcy filing/plan termination
      - 4062(e) "downsizing liability" negotiations
      - "Early Warning Program" negotiations

A Brief Introduction to PBGC (Cont.)

- PBGC monitoring/reporting
  - "Early Warning" ("Risk Mitigation") Program
    - PBGC monitors corporate transactions
    - Key PBGC threat: involuntary termination
  - Annual employer reporting
  - Reportable events
  - Reporting of missed contributions totaling $1M+ (statutory lien on all controlled group property)
  - Reporting of ERISA Section 4062(e) events

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DB Plan Funding: Challenges and Options

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DB Plan Funding: Perfect Storm #2

- Skyrocketing contribution requirements
  - First, PPA sets the stage
    - Limits on smoothing and on use of credit balances
    - Benefit restrictions tied to funding levels
    - Faster amortization (many plans)
  - Then, economy takes center stage
    - Unprecedented market losses in 2008
    - Unprecedented financial challenges for employers
  - Now, contributions doubling (or more) for many plans

DB Plan Funding: Perfect Storm #2 (Cont.)

- Watson Wyatt Pension 100 Study
  - Compared year-end 2007 to year-end 2008 for 100 largest publicly-traded US pension sponsors
  - Funded ratio went from 109% to 79%
  - Aggregate funding fell by over $300 billion, from $86 billion surplus to $217 billion deficit
- Milliman 100 Pension Funding Index
  - January/February asset losses for 100 largest plans sponsored by US public companies totaled $103 billion
  - Offsetting reductions in liabilities (due to increases in discount rates) totaled $47 billion
  - Net losses for January/February totaled $56 billion

DB Plan Funding: Perfect Storm #2 (Cont.)

- Limited relief in Worker, Retiree, and Employer Recovery Act of 2008 (“WRERA”)
- Further legislative relief sought
- Regulatory relief also possible

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DB Plan Funding: Options

- Hope for the best (but “hope is not a strategy”)
  - Hope for legislative relief
  - Hope for market to recover
  - Hope for increasing interest rates
- Freeze plan (if not already frozen)
  - Limited contribution effect, particularly for legacy plan
  - Replacement benefits may offset some/all savings
- Explore with actuary whether any permissible choices, assumption changes, etc., may help

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DB Plan Funding: Options (Cont.)

- Consider funding waiver
  - Must show "*temporary* substantial business hardship"
  - Translation: "hardship" *and* "bounce-back"
  - If >$1M, PBGC involved and security required
  - Not a panacea
    - Must be paid back with interest over 5-year period
    - Repayment in addition to regular requirements
    - IRS likely to grant subject to "conditions" (*e.g.*, repayment ahead of 5-year statutory schedule)
    - If conditions not met, waiver retroactively nullified
    - Limit of 3 waivers for any 15-year period
- Consider distress termination (see later slides)

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PBGC's Pursuit of "Downsizing Liability" (ERISA Section 4062(e))

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PBGC's Stepped-Up Enforcement of 4062(e) Liability

- PBGC's 2008 Annual Report reports that, in FY 2008:
  - "PBGC expanded its efforts to negotiate additional protections for underfunded plans in certain corporate downsizing events"
  - "PBGC negotiated settlements with five companies," including Electrolux Home Products ($77.5M) and Elkem Metals ($39.3M)
- FY 2009 to date:
  - PBGC announced settlement with Visteon Corporation ($55M)
  - Cited as "an example of our continuing, aggressive efforts on behalf of workers and retirees in the pension plans we insure"
  - Per January 27, 2009, media report (morningstar.com): PBGC then had "roughly 50 active cases"
- PBGC's stepped-up enforcement tied to mid-2006 regulatory "fix" and recent spate of downsizings

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PBGC's Stepped-Up Enforcement of 4062(e) Liability (Cont.)

- Trigger
  - "Cessation" of "operations" at a "facility" in any "location"
  - As "result" of cessation, > 20% of plan's active participants are "separated from employment"
- Liability amount
  - Pre-2006 reg "fix": 100% of PBGC termination liability
  - Post-2006 reg "fix": PBGC termination liability x headcount reduction percentage
- Satisfy liability with escrow or "up to 150%" bond
  - If distress or PBGC-initiated termination within 5 years, escrowed funds or bond proceeds added to plan assets
  - Otherwise, bond cancelled or escrowed funds returned (*without* interest)

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PBGC's Stepped-Up Enforcement of 4062(e) Liability (Cont.)

- Many unresolved interpretive issues re 4062(e) re:
  - Applicability to asset or stock sales
  - "Facility"
  - "Location"
  - "Operations"
  - "Cessation"
  - "Result of"
  - "Separated from employment"
- Little or no PBGC guidance on these issues
- Virtually no case law (minimal activity before 2006 reg "fix"; settlements rather than litigation since then)

PBGC's Stepped-Up Enforcement of 4062(e) Liability (Cont.)

- Resolution likely to be through settlement with PBGC
- Settlement options might include:
  - Additional contributions
  - Waiver of existing credit balance
  - Grant of security interest
  - Letter of credit
  - Escrow with interest
  - Guarantee from foreign CG member
  - Guarantee from non-CG member
- Watch out for *separate* reporting requirements (reportable event *and* ERISA Section 4063(a))!

“Early Warning Program” Negotiations

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“Early Warning Program” Negotiations

- “Early Warning Program”
  - Also called “Risk Mitigation Program”
  - Focus: increased risk resulting from corporate transactions
- PBGC staffing: financial analysts, actuaries, accountants, and attorneys
- Controlled group liability is key
- Determining controlled group status
  - Parent-sub group: 80% ownership of sub by parent
  - Brother-sister group: 5 or fewer individuals, estates or trusts own 80% of 2 or more businesses
  - Combined group: group with both brother-sister and parent-sub components
  - Extensive rules re attributed ownership and excluded interests

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“Early Warning Program” Negotiations (Cont.)

- Joint and several controlled group liability
  - *Each* member liable for full amount
  - Applies to:
    - Unpaid contributions and related excise taxes
    - Ongoing/termination premiums (and penalties/interest)
    - Plan termination liability (unfunded benefit liabilities)
    - Certain information penalties under ERISA Section 4071
  - PBGC liens ($1M+ missed contributions; portion of unpaid termination liability) can reach all CG property
- All CG members considered in distress/PBGC-initiated terminations

“Early Warning Program” Negotiations (Cont.)

- Consider contacting PBGC first (where contact is inevitable, it may be that the earlier, the better)
- PBGC concerns
  - Breakup of controlled group (*e.g.*, sale of “crown jewel” subsidiary)
  - Transfer of plan to weaker controlled group
  - Movement of value between/among CG members
  - Highly leveraged transaction

“Early Warning Program” Negotiations (Cont.)

- PBGC leverage
  - PBGC-initiated termination (the “nuclear” option)
  - “Evade or avoid” lawsuit
- Your leverage
  - Save jobs (political/public relations leverage)
  - Plan *will* continue (financial leverage)
- Settlement possibilities include:
  - Additional contribution to plan
  - Retention of plan by strong seller
  - Guarantee by seller if future plan termination
  - Transfer to plan of security interest

Distress Terminations

Distress Terminations

- If plan is underfunded, only way to terminate voluntarily is through "distress termination"
- *Each* controlled group member must meet at least one test:
  - Distress Test 1: Liquidation in bankruptcy/insolvency
  - Distress Test 2: Reorganization in bankruptcy
  - Distress Test 3: Inability to continue in business
  - Distress Test 4: Unreasonably burdensome pension costs
- Each CG member may meet different test
- Distress terminations usually arise in bankruptcy setting (liquidation/reorganization)
- Collective Bargaining Agreement can block distress termination (subject to 1113 motion to reject CBA)

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Distress Terminations (Cont.)

- Liquidation distress test (Test 1): automatic
- Reorganization distress test (Test 2): often contested
  - Show "meaningful sacrifices" in all areas
  - Show plan unaffordable even w/freeze & waiver
  - If lender/investor insists on plan termination, show:
    - Lender/investor has sound financial basis
    - Inability to find lender/investor not insisting on termination
  - Multiple plans: PBGC argues for plan-by-plan determination
  - Watch out for any *non-debtor* controlled group members (each one must also meet distress!)
  - Watch out for "follow-on" plans (major PBGC concerns!)

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Distress Terminations (Cont.)

- Distress permitted outside bankruptcy under Tests 3 and 4
  - PBGC makes determination
  - Can be very useful for small to mid-size employer where bankruptcy not otherwise necessary, too costly, etc.
  - Business continuation test (Test 3) analogous to reorganization test (Test 2)
  - Test 4 very rarely used to date
- Procedures
  - Various notices and filings
  - Restrictions on lump sums and annuity purchases
  - Cutbacks of benefits to estimated Title IV levels
  - No specific deadline for PBGC to decide distress

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Distress Terminations (Cont.)

- In (common) bankruptcy reorganization context, PBGC will
  - Appear in court
  - Submit brief stating its view of Test 2, and
  - Support, oppose, or take no position on distress motion
- Note PPA's "deemed" termination date of bankruptcy petition date
  - For certain purposes relating to Title IV benefit amounts
  - Not for employer liability

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PBGC-Initiated Terminations

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PBGC-Initiated Terminations

- PBGC-initiated termination (“involuntary termination”)
  - May be used/threatened to block corporate transaction:
    - Breakup of controlled group (*e.g.*, sale of “crown jewel” subsidiary)
    - Transfer of plan to weaker controlled group
    - Movement of value between/among CG members
    - Highly leveraged transaction
  - May be used (in some circumstances) to cut off increased PBGC exposure (guaranteed benefits)

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PBGC-Initiated Terminations (Cont.)

- PBGC-initiated termination (cont.)
  - Possible "triggers" include reportable event notices and "Early Warning Program" monitoring
  - Less controversial uses:
    - "Abandoned" plans
    - "Shortcut" in lieu of distress process
  - May be (and often is) done by agreement with plan administrator

PBGC-Initiated Terminations (Cont.)

- Criteria for PBGC-initiated termination
  - Minimum funding standard not met (missed annual "catch-up," not missed quarterlies)
  - Plan "will be unable" to pay benefits when due (*mandatory* termination if *currently* unable)
  - Substantial owner distribution (rare)
  - PBGC "long-run loss" determination: "the possible long run loss of the [PBGC] with respect to the plan may reasonably be expected to increase unreasonably if the plan is not terminated"
- "Long-run" loss analysis
  - Likelihood of future termination if PBGC does not act now
  - Expected increase in PBGC loss (current v. future termination)

PBGC-Initiated Terminations (Cont.)

- PBGC can quickly set termination date by publishing notice
  - "Locks in" immediate termination date and related liability
  - But subject to later court approval or agreement with plan administrator
- Termination date
  - May be retroactive
  - No earlier than when participant expectations extinguished
  - PBGC may seek later date for financial reasons
  - Subject to PPA's "deemed" termination date of bankruptcy petition date
    - For certain purposes relating to Title IV benefits
    - Not for employer liability
- CBA *cannot* block PBGC-initiated termination

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Bankruptcy Claims/Disputes

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Bankruptcy Claims/Disputes

- Key PBGC concerns
  - Adequate information in disclosure statement
  - Funding of plan during bankruptcy
  - Future of plan
    - Ongoing
    - Standard termination
    - Distress or PBGC-initiated termination
  - Treatment of PBGC claims
- PBGC bankruptcy claims
  - Many priority arguments raised by PBGC
  - Most arguments rejected by courts
  - Usually resolved with “global” PBGC settlement

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Bankruptcy Claims/Disputes (Cont.)

- Potential PBGC “post-bankruptcy” liability
  - New “exit fee” for PBGC-initiated terminations and non-liquidation distress terminations
    - $1,250 per participant, per year, for 3 years
    - For employers in bankruptcy reorganization, 3-year period starts post-confirmation
  - Challenged in court (non-dischargeable debt vs. dischargeable general unsecured claim?)
  - If upheld, may lead to more asset sales followed by liquidations

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Bankruptcy Claims/Disputes (Cont.)

- Guarantor claims
  - Unpaid premiums
    - General unsecured if plan year starts pre-petition
    - Check PBGC calculation methodology!
  - "Unfunded Benefit Liabilities"
    - Contingent on plan termination
    - Often filed as unliquidated
    - Disputes re amount: based on PBGC valuation regulation assumptions (controversial)
    - Disputes re priority: PBGC claims tax status up to 30% of aggregate positive net worth in CG, but courts have rejected

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Bankruptcy Claims/Disputes (Cont.)

- Successor trustee claims
  - Unpaid contributions
    - Contingent on plan termination and PBGC trusteeship
    - Tax status arguments ($1M+) rejected by courts
    - Post-petition "administrative" priority
      - Limited (at most) to normal cost
      - Reduce for decline in employment levels
    - Limited priority for 180-day pre-petition period
    - Rest is general unsecured
  - Fiduciary breach (not common)

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Bankruptcy Claims/Disputes (Cont.)

- Resolving claims with PBGC
  - Settlement common
  - Actuary to actuary (plan/PBGC): agree on numbers
  - Attorney to attorney (debtor/PBGC): resolve priority and (for UBL claim) amount disputes
  - End result:
    - May be single sum
    - If PBGC sees good "test case," settlement may not happen

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Questions?

Harold J. Ashner

Keightley & Ashner LLP

One Metro Center

700 12th Street, NW, Suite 700

Washington, DC 20005

www.keightleyashner.com

haroldashner@keightleyashner.com

(202) 558-5150

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February 18, 2009

CLIENT ALERT

Downsizing Employers with Ongoing Pension Plans
May Face an Immediate and Significant PBGC Liability

The Pension Benefit Guaranty Corporation—relying on an obscure ERISA provision that had been largely ignored for decades—is aggressively pursuing liability against downsizing employers with ongoing pension plans. On the books since 1974, ERISA Section 4062(e) empowers PBGC to make an immediate demand that an employer provide an escrow payment or post a bond in the case of certain cessations of its operations that result in the separation from employment of more than 20 percent of its employees who are participants in its defined benefit pension plan. Until mid-2006, when PBGC issued a final rule that established a potentially workable liability formula under this provision, there was little effort on PBGC's part to pursue this liability.

With the regulatory fix now firmly in place and with constant press reports of significant downsizings as employers grapple with an economy in turmoil by cutting back jobs or moving them overseas, this previously dormant provision has become a centerpiece of PBGC's enforcement efforts:

- According to PBGC's 2008 Annual Report (at p. 23), in FY 2008 "PBGC negotiated five settlements that provide for additional pension contributions and other protections totaling $125 million, which will help to secure the benefits of over 13,000 participants."
- In a January 15, 2009, press release, Charles E.F. Millard, then PBGC's Director, touted a recent (FY 2009) settlement for $55 million in additional protection as "an example of our continuing, aggressive efforts on behalf of workers and retirees in the pension plans we insure."
- A recent press report states that PBGC "is monitoring more than 1,100 companies" and has "roughly 50 active cases"; that PBGC's use of this provision "is being kicked into high gear as the insurer is threatened by the possibility of millions in pension liabilities being added to its books"; that in the first quarter of FY 2009 (October through December of 2008), PBGC had "already secured $60 million worth of protections"; and that PBGC "is urging companies to come to it and negotiate changes to strained pension plans before plant closures."

The statutory and regulatory framework sets forth what triggers Section 4062(e) liability, how the liability amount is to be determined, and how that liability is to be satisfied:

- *Liability trigger.* Liability under Section 4062(e) is triggered when "an employer ceases operations at a facility in any location and, as a result of such cessation of operations, more than 20 percent of the total number of [its] employees who are participants under a plan established and maintained by [it] are separated from employment."
- *Liability amount.* Under PBGC's regulation implementing Section 4062(e), the amount of the liability is the plan's underfunding calculated (using conservative PBGC plan termination assumptions) as if the plan had terminated immediately after the cessation of operations multiplied by the percentage reduction in active participants. (Before PBGC's regulatory fix, the liability under a literal reading of the statute was arguably 100 percent of the termination liability regardless of the percentage reduction in active participants.) For example, in the case of a plan that is underfunded by $200 million on a PBGC termination basis and that experiences a 25 percent reduction in active participants in connection with a Section 4062(e) event, the resulting liability amount is $50 million.
- *Methods of satisfying liability.* Under the statute, PBGC can demand that the employer provide it with an escrow in the amount of the Section 4062(e) liability ($50 million in the above example) or purchase a bond for up to 150 percent of that amount ($75 million in the above example) to protect the pension plan in the event it terminates in a distress or involuntary (PBGC-initiated) termination within the next five years. If such a termination occurs, the escrowed funds or the bond proceeds are added to plan assets; otherwise, at end of the five year period, the escrowed funds are returned (but without any interest) or the bond is cancelled.

PBGC finds out about these events through PBGC filings (both under its reportable events regulation and under ERISA Section 4063(a)) and its "early warning"/"risk mitigation" program.
There are many intricacies, including a number of unresolved interpretive issues, relating to the assertion of liability pursuant to Section 4062(e). To get a partial sense of the issues that may arise in various factual settings, consider the following sampling:

- *Applicability to "going concern" asset sales.* Under what circumstances, if any, can Section 4062

(e) liability be triggered by a "going concern" asset sale: (1) where operations "cease" *with the seller* but continue *with the buyer*; and (2) where, similarly, more than 20 percent of a plan's active participants are "separated from employment" *with the seller* but continue in employment (seamlessly in a "same-desk" situation) *with the buyer*? PBGC issued several opinion letters in the late 1970s and early 1980s concluding that there was no Section 4062(e) event in the context of various "going concern" asset sales then presented to it for consideration. Nevertheless, PBGC clearly has not given up on its ability to pursue Section 4062(e) liability for "going concern" asset sales.

- *Applicability to stock sales.* Even a stock sale might lead PBGC to take the position that a Section 4062(e) event has occurred, based on the argument that the term, "employer," under the ERISA Title IV definition, means the entire controlled group maintaining the pension plan before the sale, not just the subsidiary being sold.
- *"Facility in any location."* Can two or more buildings that are near each other together constitute a single "facility in any location"? How about two or more buildings that are far apart but that together perform a single set of fully integrated operations? Can a single building house two or more separate "facilities" for purposes of Section 4062(e)?
- *"Operations."* Can Section 4062(e) liability be triggered where only one of two or more discrete sets of "operations" at a single "facility in any location" have ceased? What is the test for determining whether two or more activities together constitute a single set of "operations"?
- *"Cessation."* How complete does the "cessation" have to be? What if a very small percentage of the "operations" continue indefinitely? What is the effect of the completion of work in progress, possibly over an extended time period?
- *Timing.* What is the date of a "cessation" that occurs gradually, or in stages, over a period of months or even years?
- *"Separation from employment" as "result" of cessation.* What if, at or near the time of the cessation, an employee retires as planned or decides to accept a job offer from another employer—or dies? How about an employee who is laid off with recall rights? Or an employee who never worked at the facility where operations are ceasing but who is arguably separated from employment as a "result" of that cessation? Consider the complete cessation of all operations at a factory with a consequent reduction in employment levels at a warehouse that had been servicing the shuttered factory and that continues to service several ongoing factories.

When PBGC becomes aware of a situation that may constitute a Section 4062(e) event, it needs to decide whether and, if so, how to pursue the matter. A negotiation will likely ensue, with the statutory and regulatory framework providing nothing more than a starting point for PBGC and the employer as they try to craft an appropriate settlement in light of the many intricacies associated with a particular factual situation. Ideally, the settlement will strike an appropriate balance that protects the pension plan while recognizing the business needs of the employer. Options for addressing any agreed-upon Section 4062(e) liability amount may include (in lieu of an escrow payment or bond) a letter of credit, additional contributions coupled with a waiver of any resulting prefunding balances, a grant of security (not necessarily a first position), or a guarantee by a foreign member of the sponsor's controlled group or by a non-controlled group member.

There are many costs that an employer contemplating a significant downsizing needs to take into account as part of the planning process. One of those costs, and in some cases the largest one by far, may be the Section 4062(e) liability. Developing a reliable estimate of the likelihood and magnitude of this liability is critical, as is evaluating whether careful planning may be able to minimize or even eliminate it.

Downsizing employers or their professional advisors who would like to discuss issues relating to Section 4062(e) liability may contact Harold Ashner (haroldashner@keightleyashner.com) or Jim Keightley (jimkeightley@keightleyashner.com) at 202-558-5150.

For further information, see "PBGC's Final Rule on Liability for Facility Shutdowns Affects Downsizing Employers" by Harold J. Ashner (Pension & Benefits Reporter, BNA, June 23, 2006) and "Beware of PBGC Downsizing Liability!" by Harold J. Ashner (Journal of Pension Benefits, Aspen Publishers, Inc., Spring 2008).

Disclaimer
One Metro Center
700 12th Street, N.W., Suite 700
Washington, D.C. 20005
T 202.558.5150 : F 202.558.5151
Site Map

PBGC ISSUES

Surprise—You Just Missed a PBGC Reporting Deadline!

PBGC reporting requirements can catch you off guard. This article highlights several "traps for the unwary" so that you won't fall into one of them.

BY HAROLD J. ASHNER

Harold J. Ashner is a partner at Keightley & Ashner LLP, a boutique law firm focusing on PBGC matters. He served as the PBGC's Assistant General Counsel for Legislation and Regulations until early 2005, when he established Keightley & Ashner LLP with James J. Keightley, the PBGC's General Counsel, and William G. Beyer, the PBGC's Deputy General Counsel. Mr. Ashner is a frequent author and lecturer, is often quoted in the media, is active in the ABA, is a Fellow of the *American College of Employee Benefits Counsel*, and is routinely retained by major law firms and employers to deal with PBGC-related issues.

Complying with PBGC reporting requirements can be tricky. The real challenge is to know whether and when to report; knowing *what* to report usually is easy. Unfortunately, missing a PBGC reporting deadline can be costly, given the exposure to penalties that could be as high as $1,100 per day for as long as the delinquency continues.

Reportable Events

The rules governing PBGC reportable events provide several opportunities for you to overlook a reporting requirement. Consider the following examples:

- *Active participant reduction.* Reporting is required if a plan's active participant count is reduced to less than 80 percent of the count at the beginning of the current plan year or 75 percent of the count at the beginning of the previous plan year. You must perform this count, at least in theory, on a daily basis, not just at the beginning or end of a plan year; it is only the *baseline* count that is tied to the beginning of a plan year. It does not matter that the reporting threshold is crossed without the occurrence of any discrete "event," such as a facility closing; normal attrition suffices. And it is possible to trigger the reporting requirement without any immediately preceding reduction in the active participant count—indeed, there may have been an immediately preceding *increase*—where the count at the beginning of a plan year is less than 75 percent of what it was at the beginning of the previous plan year. In such circumstances, reporting is required even if essentially the same active participant reduction (resulting from, *e.g.*, a facility closing during the previous plan year) has already been reported. The PBGC staff interpretation of the regulation is that each plan year starts a new reporting cycle, and that the first day of that plan year on which the active participant count is less than 80 percent of the count at the beginning of the plan year or is less than 75 percent of the count at the beginning of the previous plan year is the date on which an active participant reduction reportable event occurs. Fortunately, there are several reporting waivers and extensions available for the active participant reduction reportable event, although some apply only in circumstances where an ERISA Section 4062(e) event (generally involving facility closings, as discussed later in this article) is unlikely to have occurred.
- *Extraordinary dividend.* There is a statutory reportable event tied to the declaration of an extraordinary dividend based on the definition in the Internal Revenue Code. The PBGC by regulation has waived reporting of this statutory reportable event and, in its place, has created by regulation an "extraordinary dividend" reportable event with its own PBGC-specific definition. What is important to keep in mind, and is easy to miss, is that a transfer of value to any other member of the controlled group maintaining the plan could be reportable. This is because the regulatory event captures certain significant transfers of value to "shareholders," and a transfer to anyone in the controlled group—up, down, or sideways—is treated as a transfer to a shareholder.
- *Change in sponsor or controlled group.* One key reportable event—often thought of by practitioners as the "controlled-group breakup" reportable event, and of great importance to the PBGC because of

its various potential claims against *each* controlled-group member *on a joint and several basis*—calls for reporting when there is a transaction that results, or will result, in one or more persons ceasing to be members of the controlled group maintaining the plan. This reportable event captures not only changes in the makeup of the controlled group, such as when a parent that sponsors a plan sells a non-sponsor subsidiary to another controlled group, but also transactions where a plan is transferred (*e.g.*, in connection with the sale of a division) to another controlled group and the makeup of each controlled group remains absolutely intact; from the standpoint of the plan, every "person" that was a member of the plan's pre-transaction controlled group will cease to be a member of the plan's controlled group as a result of the transaction. This event also captures the merger of one member of the plan's controlled group into another member, even though all corporate assets and liabilities remain within the controlled group, since one of the merging entities will necessarily cease to exist as a separate entity. (Such an intra-controlled-group merger can significantly dilute the values of the PBGC's potential joint and several claims.)

It is important to keep in mind that you may not be able to wait until after the transaction has become effective to file the required report, since the event is triggered by the existence of a legally binding agreement that *will* result in the change in sponsor or controlled group. Oddly, where there is a lengthy period between the date of a legally binding agreement and a later closing date on which the transaction becomes effective, post-event reporting may be due *before* advance reporting is due! This is possible because post-event reporting is due 30 days after the date of actual or constructive knowledge that the reportable event has *occurred*, whereas advance reporting—which applies only to a very small group of privately held controlled groups with significantly underfunded plans—is due 30 days before the *effective date* of the reportable event.

- *Plan spinoffs.* Another reportable event captures certain non-*de minimis* transfers of benefit liabilities to a plan maintained by another controlled group. The regulation contains a generous waiver under which no reporting of this event is required so long as the transfer complies with the Internal Revenue Code Section 414(l) rules using PBGC "safe harbor" actuarial assumptions, regardless of how much underfunding is transferred from one controlled group to another and regardless of the relative financial positions of the two controlled groups. However, the transfer might still be reportable, not based on this reportable event, but rather based on the corresponding active participant reduction reportable event, which has no corresponding waiver tied to the use of PBGC "safe harbor" assumptions. PBGC staff takes the position that a spinoff can constitute an active participant reduction for the transferor plan, even though all of the transferred active participants involved continue to be active participants (in the transferee plan). The lesson here is to run each set of facts through all potentially applicable reportable events before concluding that no reporting is required based on a waiver that applies only to a particular event.

Notice of Missed Contributions (Form 200)

When there is a failure to make one or more quarterly or other contributions required under the minimum funding rules, and the total of the unpaid balances (including interest) exceeds $1 million, there are significant financial and reporting consequences. A statutory lien in favor of the plan arises on all controlled-group property, and within 10 days after the contribution due date, a Form 200 must be filed with the PBGC.

What you might not be aware of is that the PBGC has its own special methodology for calculating total missed contributions for this purpose—a methodology that can involve significant double-counting. Instead of using the plan's current accumulated funding deficiency or funding shortfall, the PBGC will simply bring each missed contribution forward with interest and then add them all together, even though the missed contributions for one plan year may already be reflected, at least in part, in the missed contributions for the next plan year. What this means is that there may be a Form 200 reporting obligation and, more important, a statutory lien on all controlled-group property, even though the plan's accumulated funding deficiency or funding shortfall is well below the $1 million threshold.

Notice of ERISA Section 4062(e) Event

An ERISA Section 4062(e) event occurs when an employer "ceases operations at a facility in any location" and, as a result, more than 20 percent of the active participants in a PBGC-covered plan established and maintained by the employer are separated from employment. The occurrence of such an event triggers a contingent liability (tied to plan underfunding and enforceable by the PBGC) to protect the plan in case it undergoes an underfunded termination in the next five years, as well as a reporting obligation to the PBGC under ERISA Section 4063(a).

Notice of the event is due to the PBGC under ERISA Section 4063(a) within a 60-day period. Ensuring that the required notice is timely filed can be difficult, not only because of a lack of guidance on when the 60-day period begins (*e.g.*, the date of the cessation, the date on which the 20 percent threshold is crossed, or the later of those two dates), but also because of the many unresolved interpretive issues regarding whether and when an ERISA Section 4062(e) event has occurred—issues such as whether an asset or stock sale could constitute a Section 4062(e) event, what is meant by "a facility in any location," how complete a cessation must be, when a cessation that occurs in stages or over an extended period is deemed to have occurred, and how to determine whether an active participant at the same or a different facility is treated as having been separated as a result of the cessation.

In addition, there is a potential trap here in that you might reason that, if reporting is waived or extended for the generally corresponding active participant reduction reportable event, reporting of the Section 4062(e) event is similarly waived or extended. You would be wrong; there are no waivers or extensions that apply to the requirement to report an ERISA Section 4062(e) event under ERISA Section 4063(a). Plan administrators of even the smallest and most well-funded plans—plans that would qualify for multiple waivers under the active participant reduction reportable event and that would face not even a *potential* contingent liability under ERISA Section 4062(e)—are required to report the occurrence of an ERISA Section 4062(e) event under ERISA Section 4063(a), with penalty exposure if they fail to do so in a timely manner.

ERISA Section 4010 Annual Reports

Under ERISA Section 4010 and the PBGC's implementing regulations, certain controlled groups are required to file annual reports with the PBGC containing specified financial and actuarial information. The most common trigger for reporting before PPA was that the plans maintained by the controlled group had aggregate underfunding on a PBGC premium basis in excess of $50 million. PPA repealed that trigger and, in its place, requires reporting if any plan maintained by the controlled group is less than 80 percent funded under the new PPA funding rules. The PBGC issued a proposed rule that would waive reporting based on the new PPA reporting trigger where the controlled group's aggregate underfunding does not exceed $15 million.

There are two other reporting triggers, however, that PPA did not change the substance of and that have no such $15 million controlled-group waiver: (1) where the conditions for imposing the statutory lien for missed contributions exceeding $1 million (discussed earlier in this article) have been met for any plan maintained by the controlled group; and (2) where any plan maintained by the controlled group has been granted minimum funding waivers exceeding $1 million and any portion is still outstanding. The $1 million statutory lien trigger in particular can be overlooked because of the PBGC's double-counting methodology (discussed earlier in this article) for determining whether and when the lien arises. What is important to keep in mind is that, once the statutory lien has arisen, in addition to the requirement to file a Form 200 with the PBGC within 10 days after the contribution due date, the members of the controlled group maintaining the plan will automatically become ERISA Section 4010 filers for the "information year" (generally the controlled-group-wide fiscal year) in which the lien arose. (PBGC regulations waive ERISA Section 4010 reporting, but not Form 200 reporting, if the contribution is paid within 10 days of the due date.)

Once you become subject—based on any of the reporting triggers—to ERISA Section 4010 reporting for a particular information year, it is important to mark your calendar so that you will remember to report for the next information year *even if you are not otherwise required to report for that next information year*. Why is that? Because PBGC regulations require that, if you had to report for last year (because a reporting trigger applied) and do not have to report for this year (because no reporting trigger applies), you still have to report for this year for the sole purpose of notifying the PBGC that you do *not* have to report for this year. (The purpose of the requirement is to help ensure that filers do not overlook their filing obligations.) It would be most unfortunate to face a penalty for failing to report that you need not report!

Conclusion

For many PBGC-covered plans and the controlled groups maintaining them, reporting to the

PBGC goes well beyond routine annual premium filings. A wide variety of events and circumstances, some directly involving the plan and others only the sponsor or perhaps some distant controlled-group member, can trigger a filing obligation. A solid familiarity with the PBGC's reporting rules will help to minimize the likelihood of a reporting failure.

Note: A more detailed discussion of PBGC reportable event requirements is available at http://www.keightleyashner.com/publications/Events_JPPCwinter07.pdf. *If the reader is interested in a more detailed discussion of ERISA Section 4062(e) events, see the spring 2008 issue of the* Journal of Pension Benefits *or* http://www.keightleyashner.com/publications/PBGC-DownsizingSpring08.pdf. ■