

## QUESTIONS AND ANSWERS WITH THE PBGC

### PBGC Premiums

1. Please describe the current status of the PBGC's premium audit program.

- What is the scope of the program? How many audits have been performed during the last year, what is the range of collections and what is the rate of penalties imposed?
- How many plan years are audited?
- What information must a plan administrator provide and do auditors recognize the administrative costs and difficulty in obtaining it?

**Answer:**

The PBGC declined to give detail on how many audits had been performed recently or the rate of penalty assessment. The PBGC indicated that it was using five primary contractors to conduct the audits. Since the program commenced, \$6 million in interest, penalties and premiums had been collected, with \$1.4 million collected thus far in the fiscal year beginning October 1, 1997. In the PBGC's view, the program is doing well as an enforcement mechanism.

In an audit, information covering the past three years will be requested, but the PBGC reserves the right to go back six years if the findings regarding the first three years are significant. The attachment to the premium letter sets forth the information request, and includes the following:

- Form 5500s and all attachments (including financial statements)
- executed copies of plan amendments and attachments
- actuarial valuation reports
- IRS Forms 6559 or equivalents
- census data for actives, terminated vested, vested and nonvested participants

The census data is used to create participant worksheets to verify participant counts on the PBGC Form 1. The PBGC sometimes accepts alternative methods of calculating participant counts, if detailed census data is unavailable, but it did not describe what such alternative methods are.

Sponsors are given 45 days to respond and can obtain an automatic 45 day extension. Requests for additional time will be considered, but the PBGC considers these on a case by case basis.

2. Please describe the status of the premium "self-audit" program currently under development by the PBGC.

- How would it protect premium payors?
- What would a payor be required to do?
- What does PBGC expect the cost of such a service to be (within a range)?

**Answer:**

The self-audit program is still in proposed form and under development. ERIC and the Academy of Actuaries are commenting on a draft of the PBGC's proposal. One of the issues under consideration is what incentive to give employers to participate in the self-audit program.

Under the self-audit program, sponsors would elect to participate in the program; if such sponsors were eventually selected for audit by the PBGC, the PBGC audit would be limited in scope (basically methodology only would be audited). If errors were discovered at that time, the program might provide relief from penalties, but that is under consideration and is not final. Recent changes in the audit program may have made the need for the self-audit program less necessary and less

in demand by employers. On the other hand, employers should have a systematic way of retaining the data used in preparing the participant counts, regardless of whether they participate in any self-audit program that may be established.

3. If unfunded vested benefits, for premium purposes, were calculated in the same manner as current liability for plan funding purposes, would the PBGC's funding be undermined in any serious way? (the questioner suggests that this approach would promote simplification by eliminating an actuarial step in allaying the confusion bred by having multiple "present values" for the same benefits in order to promote simplification).

**Answer:**

The PBGC responded to this question by observing that the variable rate premium will decline significantly in 2000, as the interest rate used in the calculation will increase to 100% of the 30 year "spot rate" on Treasury bonds, and assets will be valued at full market value. The PBGC observed that the interest rate on 30-year Treasuries used for funding purposes is calculated on the basis of a moving average, and not a spot rate. This difference is attributable to a legislative decision to make the interest rate used for funding purposes be less volatile.

4. Although "church plans" are normally excluded from PBGC coverage, an "electing" church plan (under Section 410(d) of the Code) will become a covered plan. According to the IRS regulations, a church plan elects by filing a statement attached to the Form 5500. Of course, a Form 5500 is normally filed at least seven months after the close of a plan year. For coverage and premium purposes, when would such an election become effective? When would premiums for an electing church plan be treated as due and when would premiums be treated as delinquent?

**Answer:**

The PBGC declined to answer; this question is the subject of a pending request for advice.

**Standard Terminations**

5. Please describe the procedures that PBGC employs in post-termination audits. In particular, what issues does the PBGC representative focus on? What are the most frequently identified problems?

**Answer:**

On a twice yearly basis the PBGC audits a statistically significant number of all closeouts completed in the immediately preceding 6 months. The post-distribution certification is the signal that the termination is to be placed in the audit pool. Once the termination is selected for audit, the PBGC sends a letter to the sponsor requesting information, including census data and benefit calculations. The PBGC then audits a statistically significant number of benefit calculations.

Common errors found in audits are: the use of the wrong interest rate, use of a mortality table other than the table specified in the plan, elections not being sent to participants, not picking up all participants in the distributions, and not preserving all benefit options.

6. In a post-termination audit, what does PBGC require if lump-sum interest rates were too high (benefits were too low) or if rates were too low (benefits were too large)?

**Answer:**

If insufficient benefits are distributed, the PBGC will require the sponsor to make the participants whole; if excess benefits are distributed, the Agency will issue a statement that changes are not required.

7. Has PBGC taken action to invalidate a completed plan termination where it determined on post-termination audit that the notice of intent to terminate or the notice of plan benefits did not satisfy all PBGC rules?

**Answer:**

No action taken to invalidate a termination.

8. Does PBGC intend to publish a standard termination timeline to assist practitioners?

**Answer:**

There is a timeline in the standard termination instructions.

9. What instructions has the PBGC given its personnel as to how to determine a plan's "benefit liabilities" for standard termination purposes?

**Answer:**

The only definition of benefit liabilities is available in the instructions to the standard termination forms, and this definition cross-references the definition used for federal income tax purposes.

10. Does PBGC plan to continue to publish the "grandfathered" lump-sum conversion rates after 1999?

**Answer:**

No decision has been made regarding whether or not the PBGC will continue to publish the "grandfathered" lump sum conversion rates after 1999. During the next few months, the PBGC plans to publish a notice in the Federal Register soliciting comment on this issue. The PBGC said that although plan sponsors could not count on the rates being published, the PBGC expressed a distinct reluctance to cease publication without ample advance warning beyond 2000 and opportunity to consider the issues involved in ceasing publication.

The PBGC acknowledged that the UP-84 mortality table is becoming outdated, and as time passes the PBGC interest rates accordingly make less and less sense. One possibility mentioned by the PBGC is that the PBGC will stop using the rates but will continue to publish them to accommodate employers who would face significant problems under section 411(d)(6) or other problems without the rates being available. The PBGC is interested in hearing from employers about the issues they would face, but the PBGC believes that employers who simply want to subsidize lump sums could do so without PBGC rates, using a much more realistic measure. It may even be that legislation would be required to address some of the section 411(d)(6) issues, but the PBGC would not want to participate in creating a bottleneck in resolving them.

**Reversions**

11. What is the PBGC's position on whether the adoption of GATT lump-sum factors is an amendment that increases an employer's reversions, and therefore must be disregarded if it takes place less than 5 years before a plan terminates (see *Ramsey v. Amfac, Inc.*, ND Cal. 1997)?

**Answer:**

In the past, the PBGC has taken the position that an amendment that changes actuarial factors and thereby increases an employer reversion is **not** the type of amendment that would have to be disregarded under ERISA section 4044, if the amendment was effective within the five years prior to plan termination. The PBGC took that position in instructions to standard termination forms (1990-93) that are now superseded. The PBGC did not participate in the *Ramsey v. Amfac* case because the PBGC was unaware of it. However, PBGC officials suggested that the IRS could view this type of reversion as triggering an exclusive benefit violation.

12. If a contributory plan terminates with surplus assets, should the participants' share of the surplus be determined net of benefits that have already been distributed? The regulations under Section 4044 appear to indicate that category 2 benefits are determined net of benefits attributable to employee contributions that have already been distributed. Should such employees' share of the plan's surplus be reduced by the contributory benefits that have been paid out?

**Answer:**

The PBGC declined to answer; the subject of this question is also the subject of a pending request for advice.

**Transactions to Evade Liability**

13. Please describe any activity in the past year (interpretive or enforcement) involving transactions to evade liability under Title IV (Section 4069).

**Answer:**

The only case mentioned by the PBGC is the *White Consolidated* case. The parties are waiting for a decision over a year after the trial finished and post-trial briefs were filed. No other litigation under Section 4069 of ERISA has arisen; the PBGC considers cases in which it can find a clear "paper trail" documenting the specific intent of the sponsor to "dump" pension liabilities on the PBGC. Such a record was present in the *White Consolidated* case, according to the PBGC.

**Missing Participant Program**

14. The missing participant program addresses hard-to-hard find participants who can be identified and whose benefits can be determined. What should the sponsor do with respect to participants who do not fit that category (e.g., a group that the company knows was at one time covered, but for whom no records can be found)?

**Proposed Answer:**

If, after a diligent search, the employer can find no records to establish the dimension of liability to this group, it is unlikely that a potential beneficiary will be able to do so. Where some data may be available (e.g., there is pay and service data but no ages) the employer should transfer liabilities to the PBGC based on a good faith estimate. If the participant is found after the termination has been completed, or if benefits are ultimately determined that differ from the good faith estimate, the PBGC will guarantee these benefits and there will be no additional liability on the employer.

**Answer:**

The PBGC said that it was not prepared to embrace the proposed answer, as a plan sponsor has other options, including merging the portion of a terminating plan covering missing participants into an ongoing plan.

15. Where an employer maintains several defined benefit plans and terminates only one, may the employer merge the portion covering missing participants into an ongoing plan (assuming compliance under Section 414(1))? Is there any bar on spinning-off assets and liabilities after the plan termination date and merging it into the ongoing plan?

**Proposed Answer:**

It is generally preferable for a missing participant who is later identified to deal directly with his former employer rather than with the government. There is no policy reason requiring the PBGC to take over if the employer remains in a position to protect the participant's benefit if it should so choose.

**Answer:**

As indicated in the answer to the previous question, merging benefits accrued under a terminated plan with another plan is permissible. The PBGC noted that usually this should not be necessary, as the PBGC has been able to locate every participant it has sought, without exception.

**Reportable Events**

16. What is PBGC's recent experience in imposing delinquent reporting penalties under Section 4071? Have penalties been imposed in reportable events situations? In other situations?

**Answer:**

The penalties imposed under ERISA section 4071 may reach \$1100 per day, but in accordance with the PBGC's published Policy on Penalties, the penalties usually amount to \$25 per day. In the area of reportable events, greater penalties are imposed if there is a willful failure to report or if the PBGC suffers increased risk by reason of the failure to report. Such an increased risk might exist in cases of advance reporting companies or where Form 200 is not filed. The failure to file Form 501 in the standard termination process is no longer the subject of significant penalties, as changes in the standard termination process have made it easier to comply with the rules.

17. Under what circumstances, if any, does the PBGC take the position that the 30-day after-the-fact notice commences with the execution of the contract to effect a sale of assets which creates a reportable transfer of plan assets and liabilities, as distinct from the closing of the corporate transaction?

**Answer:**

Under PBGC Reg. Sec. 4043.29, if a contract creates a reportable event, the 30-day period for reporting the event begins on the date the contract is signed, not the date of the closing of the transaction. However, in the case of a transfer of assets and liabilities which creates a reportable event, the 30-day period begins on the date of the transfer. See PBGC Reg. Sec. 4043.32. The date of the transfer is determined under Code section 414(l) and the regulations thereunder on the basis of all facts and circumstances.

**Multiemployer Plans**

18. ERISA '4001(a)(3) defines "multiemployer plan," essentially, as a plan to which more than one unrelated employer is required to contribute pursuant to bargaining agreements, and provides further that a plan remains a "multiemployer" plan after termination if it was multiemployer for the plan year before termination. This assures that a plan will stay in the multiemployer system after termination even if it loses all but one of its contributing employers.

- (a) If all but one employer drops out of a multiemployer plan before it terminates, does it become a single employer plan? How long must a one-time multiemployer plan have only one contributor before it is reclassified as a single-employer plan?
- (b) Can a one-time multiemployer plan preserve its multiemployer status by adding contributing employers retroactively?

**Proposed Answers:**

(a) A multiemployer plan converts to a single employer plan if, for an entire plan year, no more than one employer is required to contribute. The change is effective for the plan year following the first year in which the plan had only one contributor.

(b) A multiemployer plan can preserve its status if it adds contributing employers retroactively, including by retroactive merger. Adding contributors retroactively means they are required to contribute for a plan year, and their participants earn service credit for a plan year, prior to the actual year in which the CBA establishing the relationship is entered. This may be achieved by adding new contributors, or by merging into another plan with separate contributing employers. Since it is highly undesirable to have a plan flip-flow between single and employer and multiemployer status, for reasons spelled out when the definition of "multiemployer plan" was streamlined in 1980, a plan that inadvertently slips into single employer status should be given some leeway to maintain its character as a multiemployer plan.

**Answer:**

The PBGC declined to answer; the subject of this question is also the subject of a pending request for advice.

19. ERISA sections 4231(b)(2) and 4232(b) require benefit-preservation in the event of a spinoff from a multiemployer plan to another multiemployer plan or to a single-employer plan. Specifically, both sections say the transaction is allowed only if, among other things, no participant's or beneficiary's accrued benefit is lower immediately after the transaction. PBGC regulation \_4231.4 says, in this connection, "a plan that assumes an obligation to pay benefits for a group of participants satisfies this requirement only if the plan contains a provision preserving all accrued benefits."

Nothing in the above language seems to prohibit splitting participants' benefits and transferring one or more parts to other plans, while making sure that the sum of the parts is at least equal to the original accrued benefit (like a stock split, for instance). Thus a plan could be divided in half, sending half of each participant's accrued benefit (along with adequate assets to provide funding security) to another plan. The transferee plan would guarantee to preserve all accrued benefits that it receives, to satisfy the regulations. Is this permissible?

**Answer:**

The PBGC stated that a transferred benefit can be bifurcated in a multiemployer plan, with plan benefits being transferred to one or more plans. Reg. Sec. §4321.2.

**Litigation**

20. Please describe significant new PBGC litigation in the past year that has set (or is likely to set) important precedent that should be of interest to benefits attorneys who are not full-time litigators.

**Answer:**

The PBGC filed an amicus brief asking the U.S. Supreme Court to hear the appeal of the 9th Circuit decision in *Hughes v. Jacobsen* on the Title IV issue. Cert. has been granted in that case. The issue of interest to the PBGC is whether or not a concept of constructive termination can exist under Title IV of ERISA. The PBGC's position is that the sole method of terminating a plan is pursuant to Title IV and the applicable regulations, and that accordingly, plaintiffs' claim that a plan amendment that had the effect of using "surplus" "attributable" to employee contributions should be denied.

The PBGC also mentioned two cases to be heard by the 10th Circuit during the week of May 18, regarding bankruptcy issues. In the *CF&I Steel* litigation, at issue is the treatment of the PBGC claims in bankruptcy. The issue in the *Bailey* case is whether a claim for termination liability is entitled to priority as a tax lien in bankruptcy.

*Dikus v. PBGC* (10<sup>th</sup> Cir.), involved the denial of shutdown benefits on sale of unit and the rehire of the employees. The court held there was no permanent shutdown of the facility.

The PBGC also discussed the most recent litigation involving its work with Pan Am. Plaintiffs had filed a class action against the PBGC with miscellaneous complaints about the PBGC's administration of the terminated Pam Am plans. In January, the district court dismissed the entire complaint, except for the claim that the PBGC had unreasonably delayed issuing IDLs (individual determination letters). The PBGC expects to defend this claim successfully, as no participant in pay status has ever had any payment from the trustee Pam Am plans.