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PENSION PLAN TERMINATIONS

by

Ron Gebhardtsbauer, FSA, EA, MAAA
and
Eric Freden, FSA, EA, MAAA

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TABLE OF CONTENTS Page

Illustrations and Charts

I. INTRODUCTION AND HISTORY

Title IV of The Employee Retirement Income Security Act of 1974 (ERISA: PL 93-406) created an Insurance Program for defined benefit pension plans. In fact, the history of ERISA will show that the pension losers in Studebaker's pension plan were a major reason for the enactment of ERISA.[1] The Insurance Program is administered by the Pension Benefit Guaranty Corporation (PBGC).

The purposes of the PBGC can be found in ERISA 4002 and are as follows:

(1) to encourage the continuation and maintenance of voluntary private pension plans for the benefit of their participants,

(2) to provide for the timely and uninterrupted payment of pension benefits to participants and beneficiaries under plans to which this title [Title IV] applies, and

(3) to maintain premiums established by the corporation under section 4006 at the lowest level consistent with carrying out its obligations under this title [Title IV].

Prior to ERISA, participants in terminated underfunded plans did not always receive all of their accrued benefits. Plan documents typically only promised benefits to the extent funded. Whether all employees knew about the caveats on their pension promise is doubtful. Knowledgeable participants, of course, encouraged strong, conservative funding.

Title IV guarantees that participants in most plans will receive their basic pension benefits up to a maximum. Recent benefit increases may not be fully guaranteed, and certain types of benefits are not guaranteed by the PBGC, such as lump sums and early retirement benefits for which the eligibility conditions have not been satisfied. The funds needed to pay these guarantees are provided through premiums from covered plans, assets of terminated plans, and collections on claims against the plan sponsors.

The following pages discuss some of the history of the Insurance Program along with the changes made through legislation.

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[1] ERISA: The First Decade; Chapter 1: "Why Was ERISA Enacted?" by Michael S. Gordon, Esq., aide to Senator Javits (Senate Labor Committee). The original ERISA never gave anything to the "pension losers" at Studebaker or other pre-1974 underfunded terminated plans. A bill before Congress in 1991 would have had the PBGC pay benefits of $6.25/mo. times years of service to these pre-ERISA "Pension Losers". Since it was to be paid out of PBGC's off-budget trust funds, it would not have affected the US annual budget, which Congress liked. However, the Executive Director of the PBGC pointed out that it could cost the premium payers $500 million dollars. It didn't pass.

MPPAA: Multiemployer Pension Plan Amendments Act of 1980 (PL 96-364 enacted 9/26/80) - Congress left a glaring hole in Title IV concerning multiemployer (M-E) plans. Even though M-E plans had to pay premiums, the PBGC was instructed not to pay their guaranteed benefits until January 1, 1978, except in certain discretionary instances. Another M-E problem with the original Title IV was that an employer could pull out of a very underfunded M-E plan without contributing to its share of the underfunded amount. Congress kept putting off these problems until it passed MPPAA in 1980. This complex amendment to ERISA solved the problems (and more) by:

(1) determining the method by which a withdrawing employer's liability to the M-E plan would be determined and paid for;

(2) allowing M-E plans to reorganize: reduce certain benefits temporarily and increase the minimum contribution (reduced if overburdened with retirees) so that they could become better funded;

(3) mandating payment of guaranteed benefits for multi-employer plans, with payment triggered by plan insolvency;

(4) allowing the PBGC to give financial assistance to insolvent M-E plans (instead of taking them over) with reasonable terms for payback;

(5) reducing the benefit guarantees for M-E plans and increasing their premiums over nine years from $.50 to $2.60 per employee;

(6) reducing the 40-year and 20-year amortization periods for past service liability and experience gains and losses to 30 and 15 respectively - the same as for single employer (S-E) plans;

MPPAA also affected both the S-E and M-E programs by the following:

(1) It forced the PBGC to guarantee benefits that are nonforfeitable under ERISA, even if the plan was not yet amended to include such benefits.[2]

(2) It repealed the Contingent Employer Liability Insurance (CELI) program. No private insurance company wanted to insure an employer's liability to the PBGC.

DEFRA: Deficit Reduction Act of 1984 (PL. 98-369 enacted 7/18/84) contained a provision which repealed MPPAA's retroactive date which imposed withdrawal liability before 9/26/80, because of concerns over its constitutionality.

SEPPAA: Single Employer Pension Plan Amendments Act of 1986 (PL 99-272 signed 4/7/86) The PBGC's deficit increased uncontrollably, so Congress passed SEPPAA as part of the Consolidated Omnibus Budget Reconciliation Act of 1986 (COBRA) 4 years after it was introduced. This amendment to ERISA changed Title IV in the following ways:

(1) It increased single employer (S-E) plan premiums to $8.50 per participant.

(2) It tightened up the rules to make it more difficult to terminate an underfunded single-employer plan (generally, an employer must be in bankruptcy to terminate an underfunded plan). This is called a Distress Termination. Alternatively, a plan could

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[2] For example, prior to MPPAA, if a plan had not yet amended its vesting rule to comply with ERISA, then PBGC only guaranteed benefits that were vested under the plan. In 1995, PBGC settled the nationwide Page/Collins v. PBGC class action suit to pay such aggrieved pension losers, per PBGC News Release 96-21, 12/27/95. This includes participants in plans that PBGC never trusteed, because the plans were "sufficient" under PBGC's rules at the time. In a 1980's court case (Rettig v. PBGC) the plaintiff argued that an ERISA mandated plan amendment that increased benefits, through improved vesting, should be automatically and immediately 100% phased-in on the ERISA date. The PBGC phased them in 20% per year. A settlement was made which picked a compromise between the two positions. PBGC now guarantees ERISA-mandated benefit improvements 100% immediately on the ERISA mandated effective date to avoid future Rettig/Page/Collins-type suits.

terminate under Standard Termination rules if it was sufficient for Benefit Commitments (generally, vested benefits).

(3) It increased the employer liability payable to the PBGC from 30% of net worth (often zero) to 75% of the unfunded guaranteed benefits.

(4) It made the former controlled group of a plan sponsor liable to the PBGC if a principal purpose of their transaction to spin-off a plan was to evade liability. (The plan termination must occur within 5 years.)

(5) It held the controlled group (CG) jointly and severally liable for the Plan Asset Insufficiency (PAI) claim and for Due and Unpaid Employer Contributions (DUECs).

(6) It created a mechanism in 4049 for participants to recoup some of the cutbacks in their benefits (because the PBGC guaranteed benefit was less than their vested accrued benefits) by giving them a claim in bankruptcy for their cutbacks.

(7) It mandated an earlier Notice Of Intent to Terminate to employees and other affected parties.

PPA: Pension Protection Act in OBRA87 (PL 100-203 signed 12/22/87) - The single employer insurance program's deficit still increased rapidly (primarily due to large failures in the Steel Industry) showing that SEPPAA was too little and too late. Thus, the Pension Protection Act (in the Omnibus Budget Reconciliation Act of 1987 - OBRA87) was enacted on December 22, 1987 to (among others):

(1) Strengthen the funding rules of §302 of ERISA (Code §412) for underfunded plans by amortizing unfunded current liabilities over 18 years and new liabilities even faster (the lower the funded ratio the faster the amortization). Prior to PPA, underfunded plans could amortize liabilities from benefit improvements over 30 years (i.e., longer than the time period over which a retiree benefit improvement would be paid out - thus draining the plan's funds);

(2) Amortize experience gains and losses over 5 years, and gains and losses due to changes in assumptions over 10 years.

(3) Require sponsors to pay their contributions quarterly and allow the PBGC to impose 412(n) liens on the controlled group for large missed contributions (a powerful tool that PBGC can use to increase their secured claims and priority unsecured claims in bankruptcy);

(4) Reduce the use of contribution waivers (hardship must be temporary and only 3 waivers allowed every 15 years) and speed up the amortization of waivers (15 years changed to 5 years);

(5) Make the whole controlled group responsible for funding the plan and for PBGC premiums;

(6) Increase the S-E premiums to $16 per participant plus $6.00 per $1,000 of underfunded vested benefits up to a maximum premium of $50 per participant.

(7) Tighten up the rules on employer reversions.

(8) Allow assets to revert to the employer only after *all Benefit Liabilities* of the plan have been satisfied. Formerly it was just *Benefit Commitments*.

OBRA87 also improved the PBGC's position with respect to terminated plans as follows:

(1) Large plans that are funded below 60% will have to post a bond before benefits can be improved by amendment.

(2) The PBGC claim was increased to the full amount of unfunded benefit liability: The PBGC's portion of the claim is the unfunded guaranteed benefits.

(3) The 4049 mechanism created by SEPPAA was eliminated. Now the PBGC submits a claim for 100% of the unfunded benefit liability and shares collections with the participants in proportion that the PBGC's claim (unfunded guaranteed benefits) is to the participants'

claim (outstanding benefit liabilities). The OBL are the value of participant's benefit not paid by PBGC. The PBGC pays the participants' portion out according to the 4044 allocation process.

(4) The priority status of PBGC's claims in bankruptcy proceedings was improved.

(5) A company in Chapter 11 bankruptcy reorganization now needs to show that liquidation would necessarily follow if the pension plan were not terminated.

The PBGC deficit still increased rapidly (primarily due to terminations in poorly-funded plans from the Airline industry - such as Pan Am and Eastern Airlines). Why were plans still underfunded 18 years after ERISA's enactment? Some reasons were:

1. 30-year amortization of retiree benefit increases
2. 40-year amortization of initial liability
3. Contributions waived or missed
4. Annuity purchases and lump sums caused the funding ratio of an underfunded plan to go down and could even wipe out a plan's funds.
5. Declining industries could not support their large group of retiree benefits
6. Liberal assumptions used for ongoing plans become very liberal when an employer is facing difficult times (e.g. employees retire earlier with subsidized benefits, especially when windows are offered - an age 62 retirement assumption won't reflect supplements well)
7. The Unit Credit Method funds to accrued benefits, not projected benefits, so funding is always in catch up mode.
8. "Dollar x Service" Hourly plans can not fund for future amendments (which are frequent in these types of plans)
9. Sponsors can take contribution holidays by using up their Credit Balances.
10. A large asset gain reduced the contribution in 2 ways: it directly reduced the Deficit Reduction Contribution and it created a large amortization credit.
11. The deficit reduction contribution in 412(l) passed by PPA was not as strong as the PBGC proposed back then.

<u>The Retirement Protection Act (RPA) of 1994 (included in GATT: PL 103-465 enacted 12/8/94)</u> The Bush and Clinton Administrations pursued a bill to address the above problems. The bill included:

1. Stronger funding rules (effective in the 1995 Plan Year), some details of which follow.
   a. The Deficit Reduction Contribution (DRC) was separated from the old Funding Standard Account rules so that the double counting of experience gains or losses (& assumption changes) would be eliminated. Plans funded over 90% (and certain plans with volatile funding ratios above 80%) would be exempt.
   b. The top end of the interest rate corridor was lowered for purposes of the DRC to 105% of a weighted 4-year average of the 30-year Treasury rate to determine Current Liability (CL). The mortality table used in most state's group annuity reserves (currently 83 GAM male and female tables per Rev. Rul. 95-28) was required. The liability increase from this will be amortized over 12 years. An irrevocable election could be made to fund all Unfunded CL over 12 years, but then the contribution could not be less than the pre-RPA rules (which had the double counting of losses).
   c. The DRC payment on unfunded new CL increased to 30% less 0.40% x (the excess of the FR over 60%), where FR = funding ratio.

d. A transition rule limited the increased contributions to those that would increase the FR of a very underfunded plan by 3% (in 1st five years) to 5% (in 7th year) e.g., 50% funded plans on 1/1/PY, must be at 53% and 56% at PY+1 and PY+2. Plans funded over 75% would need smaller increases in the FR. If this transition rule was elected, then it could not reduce the RPA contribution below the DRC contribution under pre-RPA94 rates.

e. A solvency rule required underfunded plans to maintain liquid assets[3] equal to approximately 3 year's worth of benefit payments (plus the unfunded portion of annuity purchases and lump sum). If the minimum funds were not maintained, then lump sums and annuity purchases would not be allowed (with civil penalties for impermissible distributions). This rule was needed because PBGC had taken over plans that had run out of funds (e.g. Kaiser, Allis Chalmers, and LTV).

f. Excise taxes of 10% (100% if outstanding a year) were added onto quarterly solvency payments.

g. The interest penalty on missed Quarterly contributions was eliminated for plans with no unfunded CL in prior year. Those plans would not need to make Quarterly payments nor notify employees of such under ERISA 101(d), per Rev. Rul. 95-31.

h. All scheduled benefit increases must be recognized immediately for minimum funding (not Current Liability though).

2. PBGC would get concurrent authority to enforce minimum funding standards in PBGC-covered plans, when missed contributions exceed $1 million - ERISA '4003 (e).

3. Minimum lump sums would be calculated using (a) the 30-year Treasury bond rate and (b) the Mortality Table in the Code for Group Annuity Reserves (unisex 83 GAM - 50% male and 50% female at that time per Rev. Rul. 95-6) and no expense loading. The bill would permit this 411(d)(6) cutback. Changes must be made by the 2000 PY. Maximum 415 lump sums would also use the unisex 83 GAM table and 30-year Treasury rate below age 62 per Rev. Rul. 95-29. This change had to be implemented for the 95 PY.

4. Elimination of the 10% excise taxes when:
   a. terminating plans with 100 or fewer participants can't deduct Unfunded Current Liability.
   b. the 25% of compensation deduction is reached for DB/DC combinations (DC contribution up to 6% of pay).

5. Contributing sponsors (in addition to Plan Administrator) are now also responsible to file Reportable Events with the PBGC. The number of reportable events were increased to include when contributing sponsor or certain extraordinary dividends leave Controlled Groups (CG) with a large underfunded plan or when more than 3% of the plan's benefit liabilities are transferred outside the controlled group. Contributing sponsors of plans with large underfunded amounts must notify the PBGC 30 days in advance. Public companies were exempted from this provision.

6. Require CG members to provide PBGC financial information (including actuarial valuations) if underfunding, missed contributions, or outstanding waivers are large - ERISA 4010.

7. PBGC would have alternatives to nullifying a Standard Termination if in the interests of participants.

8. Prohibit bankrupt companies with underfunded plans from increasing benefits, unless de minimus, or in a collective bargaining agreement before bankruptcy, or necessary to meet Code qualification requirements.

9. The $53 cap on variable premium would be phased out over 3 years (20%, 60%, 100%). The mortality table required to calculate current liability would be mandated, and the required interest rate would increase.

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[3] Liquid assets include the first 36 months of unmarketable GIC payments & annuity payments per Rev. Rul. 95-31

10. Plans paying variable premiums would have to notify participants of (a) the funded status of their plans and (b) the limits on PBGC guarantees - ERISA 4011. This was meant to help employees understand that bargaining for benefits in place of wages may not be good for them since those benefit increases may not be guaranteed. Per PBGC proposed regulation 4011.3 & 4, new plans, newly covered plans, and plans exempt from the DRC because of their funding ratios would be exempt from this Notice requirement. Small plans would be exempt in 1995.
11. PBGC would take over assets and liabilities of missing participants of terminating plans that diligently searched for them and still couldn't find them. Diligent search includes requesting IRS to notify participant (at last address) to contact plan administrator.
12. Maximum guarantees for disabled participants would not be reduced if they were under age 65.
13. Distress liquidation test extended to include federal banks.
14. Allows PBGC to perfect its 412(n) missed contribution lien immediately and eliminates the $1 million exclusion.

The GATT bill to which RPA was attached also has two other pension related issues, namely:

15. A 5-year extension of the Code §420 provision that allows sponsors to transfer pension funds to a 401(h) retiree health account (as long as employers provide to retirees "substantially the same level of employer-provided coverage as in the year prior to the transfer, and
16. Rounding down of the inflation adjustments to the DB limit (currently $120,000), DC limit (30,000), 401(k) elective deferral ($9,240), and SEP Compensation Threshold ($396), etc.

These last 2 provisions along with the premium provision helped fund the GATT tariff reduction bill (i.e., made it revenue neutral).

Subsequent History: In the late 1990s, the stock market achieved extraordinary returns and the PBGC had a $10 billion surplus, due to larger premiums from RPA and fewer terminations. However, the years 2000 to 2002 brought a big drop in the stock market, unusually and persistently low interest rates, and weak companies, particularly in the airline and steel industries, shedding their pension liabilities. Currently before Congress there are bills that would make the following changes.

1. The funding rules would be simplified to have one funding method (Traditional Unit Credit), one amortization period (7 years), one rule based on Current Liability (so there would be no Full Funding Limit that would eliminate contributions and premiums if plans were funded to 90% of CL), and one interest rate (based on high-quality corporate bond rates – maybe a yield curve). Smoothing of assets and liabilities will probably be reduced and the RP2000 mortality table might be required.
2. Increasing the funding target to 100% might be phased in over 5 years.
3. The Credit Balance would grow at the same rate as the pension fund's investments, and it's use might be restricted if the plan is poorly funded.
4. Benefits would be frozen if the plan were funded less than 60% of CL.
5. The payment of lump sums might be restricted in the plan was poorly funded.
6. The funding target might be increased to a termination liability proxy (most subsidized retirement and annuity price loadings) for at-risk plans (plans sponsored by employers with poor credit ratings or plans with low funding levels).
7. Restrictions would be placed on funding non-qualified plans when a company pension plan was poorly funded.
8. Shutdown benefits would be eliminated or PBGC would phase-in the guarantee of shutdown provisions from the date of shut down.
9. PBGC Premiums would be increased from $19 to $30 per participant, and no plans funded below 100% would be able to avoid the Variable Premium of $9 per $1,000 of underfunding.
10. Disclosure to participants would be made more timely and improved to show them the trend in funding ratios.

Other laws of minor relevance are:

- Revenue Act of 1978 (PL 95-600) allowed 401(k) arrangements in profit sharing plans
- TAMRA: The Technical and Miscellaneous Revenue Act of 1988 (PL100-647 signed 10/21/88) increased the excise tax on reversions from 10% to 15%.
- OBRA 89 (PL 101-239 signed 12/19/89) eliminated the variable premium for certain plans at their full-funding limit.
- Older Workers Benefit Protection Act (PL 101-433 signed 10/16/90) prohibits an employer from providing lesser benefits to older employees (based on equal cost) and overturned the Betts decision which said that a pre-ADEA disability benefit could not be a subterfuge of ADEA.
- OBRA 90 (PL 101-508 signed 11/15/90) which increased PBGC's premiums to $19 per participant plus $9 per $1,000 of unfunded vested benefits up to a maximum premium of $53 + $19 = $72 per participant (possibly to help not only the PBGC, but also to help reduce the U.S. Annual Deficit). It also tried to put to rest the question " Who do the surplus pension assets belong to?" by increasing the reversion tax to 50% unless some of it went to participants; and created a mechanism to transfer surplus pension assets to a 401(h) Retiree Health Account.
- Unemployment Compensation Amendments of 1992 (PL 102-318 signed 7/3/92) required plans to include optional trustee-to-trustee transfers of eligible rollover contributions.
- OBRA93 (PL 103-66 signed 8/10/93) lowered the 401(a)(17) maximum compensation amount to $150,000.
- USERRA: Uniformed Services Employment and Reemployment Rights Act of 1994 (PL 103-353 enacted 10/13/94) clarified that benefits of returning Persian Gulf GI's would be as if the employee had never left employment. In particular, DB accruals and DC contributions must be continued while the employee was away - an issue left unclear in the Supreme Court's decision in Alabama Power Co. v. Davis (431 US 581, 141 BPR A-16, 1 EBC 1158). Congress felt it was clear and thus the bill is retroactive.
- Bankruptcy Reform Act of 1994 (PL 103-394 enacted 10/22/94) allowed the PBGC to serve on Bankruptcy creditor committees.
- PAPA: Pension Annuitants Protection Act of 1994 (PL 103-401 enacted 10/22/94) was passed to correct the Executive Life situation by allowing DOL and former participants to seek relief when ERISA violations involving annuity purchases occur around a plan termination.
- Pension Income Taxation Limits Act (PL 104-95 enacted 1/10/96) was passed to prohibit States from taxing former residents for pensions earned while living in their state. It only applies to qualified DB plans and payments from deferred compensation plans that are payable for life or 10 years (or if the plan is a mirror plan that provides benefits above IRS limits).
- SBJPA: Small Business Job Protection Act of 1996 (PL 104-188 signed 8/20/96) repealed 5-year averaging for lump sums, allowed workers to commence benefits after age 70½, established SIMPLE retirement plans for small employers, allowed tax-exempts (but not governments) to have 401(k)s, allowed spousal IRAs, created safe-harbor 401(k)s with simpler ADP and ACP tests, included elective contributions in compensation for §415 benefit and contribution limit rules, eliminated the §415(e) combined plans limit on benefits, etc.

- Taxpayer Relief Act of 1997 (PL 105-34, singed 8/5/97) raised the FFL to 170% of CL, allowed IRAs to pay higher Education expenses and for first time homes (up to $10,000), created Education IRAs and Roth IRAs, increased de minimus cash outs to $5,000, repealed excess distribution and excess retirement accumulation taxes, relaxed the combined DB/DC limit in §404(a)(7), etc.
- EGTRA: Economic Growth and Tax Relief Reconciliation Act of 2001 (PL 107-16 enacted 6/7/2001) increased limits for contributions and benefits to DB and DC plans, phased out the cap on the FFL, extended the deduction for UCL to small plans covered by the PBGC, eliminated the 10% excise tax on many non-deductible contributions to DB plans, made many rollover changes, gave a nonrefundable tax credit for contributions to IRA and 401(k)s and plan start up costs at small employers, improved disclosure for reductions in benefits (such as for conversions to cash balance plans), increased the limits (and other items) on Education IRAs, created a new 10% tax bracket (to give everyone an advanced refund of $300 to stimulate the economy), reduced the marriage penalty, lowered all the tax rates, reduced taxes for families with children, increased the exemption amount for the AMT, reduced estate taxes, etc. This bill sunsets in 2011, whereupon the old laws would return as if never passed.
- JCWAA: Job Creation and Worker Assistance Act of 2002 (PL 107-147 signed 3/9/02) included relief for NYC, temporarily increased the top of the range for interest rates to 120% of the average Treasury rate for 2002 and 2003 plan years, etc.
- JGTRRA: Jobs and Growth Tax Relief Reconciliation Act of 2003 (PL 108-27 signed 5/28/03) reduced the 20% capital gains and dividend tax rates to 15% (thus reducing the tax advantages of pension plans and annuities), reduced tax rates at the higher tax brackets, provided marriage penalty relief, increased child tax credit, increased the AMT exemption, etc.
- PFEA: Pension Funding Relief Act of 2004 (PL 108-218 signed 4/10/2004 just before the first 2004 quarterly was due) increased the top of the range for interest rates to 100% of the 4-year average of long-term High Quality Corporate Bonds, provided some temporary relief to airline and steel companies and the TCU pension plan, and some relief and notice requirements to M-E plans.
- Working Families Tax Relief Act of 2004 (PL 108-311 enacted 10/4/04) retroactively raised the interest rate to 100% of the Treasury rate for 4011 Notice to employees for 2002 and 2003.
- AJCA: American Jobs Creation Act of 2004 (PL 108-357 enacted 10/22/04) tightened up the rules concerning tax shelters, including non-qualified deferred compensation arrangements. For example, distributions can only be deferred to a specified date, not based on change in control of a company.

As you can see, pension laws change constantly, which makes this a difficult and complex area to stay on top of.

Other Readings

This study note is primarily intended to illustrate pension law in ERISA Title IV and the regulations of the PBGC listed below:

	ERISA TITLE IV Section	Labor Regs TITLE 29 Chapter 40	Labor Regs TITLE 29 Chapter 26	29 CFR Preambles in CCH
Premiums	4006 & 7	4006 & 7	2610	& 24,134
Annual Financial & Actuarial Information Reporting	4010	4010	2628	-
Notice to Participants	4011	4011	2627	24,233
Covered Pension Plans	4021	-	-	-
Guaranteed Benefits in S-E Plans	4022 & 4022B	4022	2613 & 2621	24,008/24,219 24,010
Plan Termination Procedures	4041 & 2	4041	-	24,157
- Distress	4041(c)	Subpart C	2616	24,157
- Standard	4041(b)	Subpart B	2617	24,157
- Involuntary	4042	4042	-	
Reportable Events	4043	4043	2615	24,045 24,177
Allocation of Assets	4044	4044 Subpart A	2618	24,058/24,012 24,202
Missing Participants	4050	4050	2629	24,171
Employer Liability to PBGC	4062 - 4	4062	-	-
- Valuation of Plan Benefits	4062 - 4	4044 Subpart B	2619	-

Relevant pension **law** can be found in the Internal Revenue Code (Title 26 of the US Code) and the ERISA sections listed above in the second column. The ERISA sections are from Title 29 of the US Code and can be found at http://www4.law.cornell.edu/uscode/html/uscode29/usc_sup_01_29_10_18.html . The whole US Code (USC) can be found at uscode.house.gov or http://www4.law.cornell.edu/uscode. When searching for a section, it helps to provide the Title number and the section heading (or the USC section number, which is the same as the Title IV section number but with the "40" replaced with "13"). The law (second column) and regulations (third column) can be found in CCH, RIA, or BNA publications, which can be obtained by going to www.cch.com, ria.thompson.com, or www.bna.com respectively.

The **regulations** can also be found in the Code of Federal Regulations (CFR) at www.gpoaccess.gov/cfr/index.html. The PBGC website also provides all of ERISA and PBGC's rules and regulations (and Federal Register notices post-1996) at www.pbgc.gov/practitioners/index.html. The

fourth column provides the pre-1996 PBGC regulation numbers and the third column provides the renumbered regulations. Proposed Premium regulation 2610 (with preamble) can be found in 57 FR 12666 (April 10, 1992) or at the back of CCH under proposed DOL regulations at paragraph 20,533B. RIA has the preamble to proposed Premium regulation 2610 at paragraph 87,549.

Preambles to the regulations can be found in CCH's Volume 3 using the above paragraph numbers in the fifth column. They can be very valuable in providing the history and reasons for the regulations. Unfortunately, the service providers did not retain the older preambles to the proposed regulations after their final regulations replaced them. They also can be very valuable. You would have to go to the PBGC or the original Federal Register pages to find them.

Instructions and Forms for paying Premiums and for filing Standard or Distress Terminations should also be read. They can be accessed by going to www.pbgc.gov/practitioners/index.html.

Additionally, a brief mention of ERISA §4022A and §§4201 through 4402 (which implements the **Multiemployer Insurance** program) is included in this study note. A more thorough discussion is included in the Multi-employer Retirement Plans: Handbook for the 21st Century" by Dan McGinn which can be obtained at www.actuarialbookstore.com or 800-582-9672.

Other valuable material can be found from the handouts at EA, SOA, CCA, ASPPA meetings.

Plan terminations from the perspective of an insurance company actuary are discussed in the article entitled "**Terminal Funding**", (TSA XXXVIII, page 169ff) and can be found at library.soa.org/library/tsa/1980-89/TSA86V389.pdf . An update of that paper is at page 10 of library.soa.org/library/sectionnews/investment/RRN0205.pdf

Finally, IRS Regulation 1.414(l)-1 regarding pension **plan mergers, spinoffs and the transfers** of assets and liabilities between plans should be read due to their connection with the asset allocation procedures of Title IV. The material in this study note presumes that the reader will become familiar with the above regulations and ERISA sections.

Note: If Section numbers are not fully described in this study note, the following hints will be helpful:

(1) Sections 4001 to 4402 are from Title IV of ERISA and are the laws that the PBGC abides by and regulates.

(2) The 2600 section of the Department of Labor's regulations were where PBGC regulations use to be found. They can be related to PBGC's Title IV Law by using the chart on the prior page. The 2600 number was sometimes preceded by 29 CFR, which stands for Title 29 in the Code of Federal Regulations. The PBGC changed their regulations so that they are now the same as the ERISA section numbers.

(3) Sections 401 to 530 are from the Internal Revenue Code (IRC) - Title 26 of the USC - and are the benefits laws that the IRS abides by and regulates.

(4) Sections 4971 to 4980G are from the IRC and are generally punitive-tax-related laws affecting pension plans.

(5) Pre-ERISA IRS regulations usually start with "1." followed by the IRC Section being discussed followed by a dash and section number of the regulation e.g. 1.401-6. Post ERISA §401(a) regulations will often have the IRC subsection and paragraph, e.g. 1.401(a)(4)-1. Temporary regulations may start with an "11."

(6) Often, you will find laws citing other parts of laws or their own section or subsection, etc. The following will help you understand the extent of the cite. For example, if the words in subsection (d) say that this provision applies to this section, it will apply to all of section 4044, but nothing else:

Act = ERISA
Title IV
Subtitle C (Terminations: per ERISA's Table of Contents)
Section 4044
subsection (d)
paragraph (3)
subparagraph (B)
clause (ii)
subclause (I)

This subclause 4044(d)(3)(B)(ii)(I) of Title IV of ERISA states how to calculate the numerator of the fraction that determines how much of a plan's surplus is attributable to employee contributions.

(7) Court cases can affect the interpretation of laws within their Jurisdictional boundaries. Many Court of Appeals cases are cited in this study note. Their Jurisdictions are as follows:

First Circuit	ME, MA, NH, Puerto Rico, RI
Second Circuit	CT, NY, VT
Third Circuit	DE, NJ, PA
Fourth Circuit	MD, NC, SC, VA, WV
Fifth Circuit	LA, MS, TX
Sixth Circuit	KY, MI, OH, TN
Seventh Circuit	IL, IN, WI
Eight Circuit	AR, IA, MN, MO, NE, ND, SD
Ninth Circuit	AK, AZ, CA, HI, ID, MT, NV, OR, WA, Guam
Tenth Circuit	CO, KS, NM, OK, UT, WY
Eleventh Circuit	AL, FL, GA
Federal Circuit	US/Federal
D.C. Circuit	Wash, D.C.

(8) The laws discussed earlier can be determined quickly from the following list. The footnotes after each section of ERISA or the Code in CCH and RIA books will help the reader learn the history of the section and the effective dates of changes to the section, which can be very helpful. Congressional Committee Reports (House, Senate, and Conference) are also helpful, but it should be noted that they (like section headings) are not equivalent to law, even though federal agencies often look to them to help in their drafting of regulations.

PENSION RELATED LAWS

Law	PL Number	Enacted	Name
ADEA 67	PL 90-202	12-06-67	Age Discrimination in Employment Act of 1967
ERISA	PL 93-406	09-02-74	Employee Retirement Income Security Act of 1974
ERISA Reorganization Plan		08-10-78	ERISA Reorganization Plan
Revenue Act of 1978	PL 95-600	11-06-78	Revenue Act of 1978
MPPAA 80	PL 96-364	09-26-80	Multiemployer Pension Plan Amendments Act of 1980
TEFRA 82	PL 97-248	09-03-82	Tax Equity and Fiscal Responsibility Act of 1982
DEFRA 84 (in TRA 84)	PL 98-369	07-18-84	Deficit Reduction Act of 1984
REA 84	PL 98-397	08-23-84	Retirement Equity Act of 1984
SEPPAA (in COBRA 86)	PL 99-272	04-07-86	Single-Employer Pension Plan Amendments Act of 1986
OBRA86	PL 99-509	10-21-86	Omnibus Budget Reconciliation Act of 1986
TRA 86	PL 99-514	10-22-86	Tax Reform Act of 1986
OBRA87 (PPA)	PL 100-203	12-22-87	Pension Protection Act
TAMRA88	PL 100-647	10-21-88	Technical and Miscellaneous Revenue Act of 1988
OBRA89	PL 101-239	12-14-89	Omnibus Budget Reconciliation Act of 1989
OWBPA	PL 101-433	10-16-90	Older Workers Benefit Protection Act
OBRA90 (in RRA90)	PL 101-508	11-19-90	Revenue Reconciliation Act of 1990
UCA 92	PL 102-318	07-03-92	Unemployment Compensation Amendments of 1992
OBRA 93	PL 103-66	08-10-93	Omnibus Budget Reconciliation Act of 1993
USERRA 94	PL 103-353	10-13-94	Uniformed Services Employment & Reemployment Rights Act
BRA94	PL 103-394	10-22-94	Bankruptcy Reform Act of 1994
PAPA 94	PL 103-401	10-22-94	Pension Annuitants Protection Act of 1994
RPA 94 (in GATT)	PL 103-465	12-08-94	Retirement Protection Act of 1994
PITLA	PL 103-95	01-10-96	Pension Income Taxation Limits Act
SBJPA96	PL 104-188	08-20-96	Small Business Job Protection Act of 1996
TRA 97	PL 105-34	08-05-97	Taxpayers Relief Act of 1997
EGTRA2001	PL 107-16	06-07-01	Economic Growth & Tax Relief Reconciliation Act of 2001
JCWAA2002	PL 107-147	03-09-02	Job Creation and Worker Assistance Act of 2002
JGTRRA	PL 108-27	05-28-03	Jobs and Growth Tax Relief Reconciliation Act of 2003
PFEA2004	PL 108-218	04-10-04	Pension Funding Relief Act of 2004
WFTRA2004	PL 108-311	10-04-04	Working Families Tax Relief Act of 2004
AJCA2004	PL 108-357	10-22-04	American Jobs Creation Act of 2004

Public Laws back to 93rd Congress (1973-74) are at http://thomas.loc.gov/bss/d109/d109laws.html

The ERISA Reorganization Plan No.4 of 1978 is at http://www.dol.gov/ebsa/regs/exec_order_no4.html

II. PLANS COVERED AND PBGC PREMIUMS

1. **Coverage - §4021**

In general, Title IV applies to all pension plans determined by the Secretary of the Treasury to be qualified plans, and all pension plans maintained by an employer or employee organization if the plan has, in practice, met the requirements for qualification during the 5 preceding years. ERISA §4021 mandates coverage for all such plans unless the plan:

- is an individual account plan (or is the part of a defined benefit plan that is an individual account plan);
- is "established and maintained" for government employees by such governments (Note, however, that under PBGC Opinion Letter 75-44, a plan that is established by a private entity but later taken over by a government entity, and thus "maintained" by a government entity would generally qualify for this exemption, even though it had not been "established" by a government entity; *see also Rose v. Long Island R.R. Pension Plan*, 828 F.2d 910 (2nd Cir. 1987). On the other hand, a plan that is established by a governmental entity and later taken over by a private entity would generally not qualify for this exemption, even though it would qualify for an exemption under Title I of ERISA. See *Hightower v. Texas Hospital Association*, 65 F3d 443 (5th Cir. 1995)
- is a Church Plan (unless the plan elects to be covered);
- is an Employee funded Plan maintained by a Fraternal organization, a VEBA, or is a trust described in § 501(c)(18);
- provided for no employer contribution after the enactment of ERISA;
- is unfunded and maintained to provide deferred compensation benefits to a select group of management or highly compensated employees;
- is maintained outside of the U.S. for the benefit of nonresident aliens;
- is a plan solely to provide benefits in excess of the limitations of IRC §415 (an excess benefit plan);
- is "established and maintained" exclusively for substantial owners (Note, however, that under PBGC Opinion Letter 90-6, a plan that is maintained exclusively for substantial owner qualifies for this exemption, even though it had not been "established" exclusively for substantial owners, and may lose qualification for this exemption if it later is maintained for at least one non-substantial owner.)
- is sponsored by an exempt international organization;
- is maintained solely to comply with worker's compensation, unemployment compensation, or disability insurance laws; or
- is maintained by a professional service employer and has never had more than 25 active participants after the enactment of ERISA.

2. **PBGC Premiums: §4006 and 4007.** Like private-sector insurance companies, the PBGC charges premiums for all covered pension plans. However, the premium obligation, as well as the PBGC's insurance obligation, is established by statute rather than by contract. This means that, if a plan is covered, premiums must be paid for the plan and the PBGC must provide insurance for the plan. These two obligations are independent of one another; failure to pay premiums does not lead (as it would in the private sector) to a loss of insurance (per PBGC regulation §4007.9) , and the erroneous payment of premiums for a non-covered plan does not lead to the creation of an insurance obligation on the part of the PBGC.

a. Single-Employer Plans. Although the PBGC's regulations impose on the plan administrator of the plan the obligation to pay the premiums and to report premium-related information, the liability

for payment of the premiums (and any related interest and penalties) is on the plan administrator and the contributing sponsor of the plan. In addition, if the contributing sponsor is a member of a controlled group, each member of the controlled group (including the contributing sponsor) is jointly and severally liable for the premiums (and any related interest and penalties). The payment may come out of plan assets (if the plan so provides) or corporate assets. In PBGC Opinion Letter 94-6, the PBGC stated that a plan administrator who distributes assets in a standard termination without satisfying the premium (and related interest and penalties) liability for the plan may be held personally liable by the PBGC. The PBGC may sue to collect premiums, penalties, and interest, and will pursue collection where appropriate by filing claims in bankruptcy proceedings.

There are two components to the PBGC premium for single-employer plans: a flat-rate premium of $19 per participant and a variable-rate premium based on the unfunded vested benefits (UVB) of the plan. Thus, the variable-rate premium measures (roughly) the PBGC's exposure (or size of a potential claim) if the plan terminates rather than the PBGC's risk (probability that there will be a claim due to financial weakness of the employer). However, the variable-rate premium is in a sense indirectly related to risk, in that weaker employers tend to have more underfunded plans. The Administration has proposed to build risk more explicitly into the PBGC premium by tying the underfunding calculation to the credit rating of the contributing sponsor and controlled group. The proposal would require the vested benefit liability to be determined assuming retirement at the earliest retirement date and the election of lump sums (if available), and to include an expense loading.

The PBGC's variable-rate premium for single employer plans equals the plan's UVB times .009. Until the mid-1990s there was a cap on the variable-rate premium, but the cap no longer applies. An enrolled actuary must certify to the variable-rate premium calculation only if the General Rule (discussed below) is used or if, for a plan with 500 or more participants, the Alternative Calculation Method (also discussed below) is used. The plan administrator must certify the premium filing and, as part of that filing, must certify as to compliance with the requirement (for the prior plan year) for certain underfunded plans to issue the Participant Notice under ERISA section 4011.

The PBGC has proposed to require large plans (those with 500 or more participants for the prior plan year) to file premium information electronically starting with the 2006 plan year, and to require all plans to do so starting with the 2007 plan year. Under the proposal, the premium payment may also be made electronically, but need not be.

Premium Snapshot Date. Both the participant count (for purposes of the flat-rate premium) and the plan's UVB are determined as of the "premium snapshot date," which is generally the last day of the plan year preceding the premium payment year (the plan year for which the premium is being paid). In the case of a new or newly covered plan, however, the premium snapshot date is the first day of the premium payment year or, if later, the date on which the plan becomes effective for benefit accruals for future service. The other exception to the general rule (that the premium snapshot date is the last day of the plan year preceding the premium payment year) is that, in the case of certain non-de minimis mergers and spinoffs that become effective at the beginning of the premium payment year, the premium snapshot date is moved from the last day of the preceding plan year to the first day of the premium payment year. This rule applies to the transferor plan in a spinoff and the transferee plan in a merger, and is designed to minimize or eliminate double counting (in spinoff situations) or non-counting (in merger situations) of participants and UVBs.

Unfunded Vested Benefits (UVB) equal the unfunded current liability [see ERISA §302(d)(7) and the definition of current liability in Chapter 3 (step 10) of this Study Note], subject to two adjustments. First, only vested benefits are taken into account in determining UVBs. Second, a different interest rate, called the Required Interest Rate ("RIR") is used to value current liability. The RIR equals 85% of the 30-year Treasury rate for the calendar month preceding the calendar month in which the premium payment year begins. However, the RIR was changed on a temporary basis for the 2002 and 2003 premium payment years to 100% of 30-year Treasuries, and was changed again on a temporary basis for the 2004 and 2005 premium payment years to 100% of a corporate bond rate. When this Study Note went to press, Congress was considering changes to the rules governing the PBGC variable-rate premium that could affect the calculation (including the RIR) for the 2006 and later premium payment years. Absent any such changes, however, the RIR would snap back to 85% of 30-year Treasuries for the 2006 premium payment year. However, under current law, Treasury has the authority to specify a new mortality table for CL. Once it does so for a plan year, the RIR to be used for PBGC variable-rate premium purposes for that and future plan (premium payment) years will be 100% of 30-year Treasuries, even though the mortality change itself would generally not affect the premium calculation until the next plan year (per Q&A 4 of the PBGC's 2000 Blue Book). In addition, the value of assets will shift from actuarial value to Fair Market Value (FMV) for any premium payment year for which the RIR is 100% of 30-year Treasuries because of the adoption by Treasury of new mortality tables for CL (per the same Q&A 4). The mortality change would serve to increase the UVB, the interest change would serve to decrease the UVB, and the effect of the change to FMV of assets will of course depend on the plan's investment experience.

Section 302(d)(7)(D) allows some service to be disregarded for certain new participants. This helps new plans that granted large past service amounts to phase-in a large variable premium. Also, according to PBGC's preamble to the proposed variable-rate premium regulation issued on October 5, 1988 (53 FR 193), contingent benefits such as 30 & Out benefits and future disability benefits are not in vested CL if a participant is not yet entitled to the benefit as of the premium snapshot date. This probably means that the value of shutdown benefits do not need to be included if a shutdown has not occurred. However, PBGC has suggested informally that the value of the QPSA should be included since it is vested per 4022(e), although technically it only applies to §4022. In addition, the value of automatic COLAs should be included, since the only way a participant could forfeit it is due to death.

One need not subtract the credit balance from the assets for premium purposes even though §302(d)(8)(E) requires it for subsection 302(d). Contributions on the prior plan year's Schedule B can only be reflected in assets if paid before the earlier of the variable-rate premium due date or payment date. If such contributions are made after the premium snapshot date, they are to be discounted back to the premium snapshot date.

PBGC Premiums (Single Employer Program)

Plan Years on or after	9-2-74 ERISA	1/1/78	1-1-86 SEPPAA	1-1-88 OBRA87 (PPA)	1-1-91 OBRA90	7-1-94 GATT (RPA)	1/1/95	7/1/95	1/1/96	7/1/96	1/1/97	7/1/97	2002-3 &2004-5 Plan Yrs	1/1/06	after new Mortality Table
Flat Rate	$1.00	$2.60	$8.50	$16	$19										
Variable Rate Premium (VRP) per $1000 of UVB [1]	No Variable Premium			$6	$9										
Maximum VRP per participant				$34 [2]	$53 [2] + percent of amount above cap in following line					Unlimited					
% of VRP over cap				0%		20%		60%		100%					
Mortality Table				Table used for funding					GAM 83 mortality table [3]						New Table[3]
Disability Table				Plan's Disability Table							IRS Disability Table [3]				
Interest Rate				80% of 30-year Treasury								85% of 30-year Treas.	120% 30-yr Tr & 100% HQ LT corp.	85% of 30-year Treas.	100% of 30-yr Treas.
Asset Val Method				Method used for funding											Fair Market

1. UVB: Unfunded Vested Benefits
2. Reduced by $3 for each year that maximum was contributed in 1983 to 1987. This rule applied for only 5 plan years.
3. The UVB calculation uses Current Liability (CL) determined at the end of the prior year. Thus, the tables are used 1 year later for premiums than for CL calculation.

See PBGC's 2001 Pension Insurance Data Book (page 59) http://www.pbgc.gov/publications/databook/

General Rule Method: The assumptions must be the same as those used in calculating the §412(l) current liability (except as otherwise provided in the PBGC's premium payment regulation, *e.g.*, use of the Required Interest Rate rather than the CL interest rate) for the plan year that contains the premium snapshot date (generally the plan year preceding the premium payment year). The asset valuation method must be the same as the one used for the §412 contribution for that plan year (until FMV is required once Treasury adopts a new mortality table). There is no requirement to do a valuation for premium purposes as of the premium snapshot date. Earlier valuations can be used as long as appropriate adjustments are made (e.g., adjustments for passage of time, significant events); however, informal PBGC guidance (Q&A 2 of the 2002 PBGC Blue Book) states that any such "roll forward" must reflect experience gains and losses (*e.g.*, significant events) between the date of the original valuation and the premium snapshot date. A valuation on the first day of the premium payment year can be used instead of the day before. If assumptions or methods (including asset valuation method) were changed and resulted in a material decrease in liability between those 2 dates, or if the results on these 2 dates materially differ for any other reason, an adjustment must be made per §4006.4(a)(2)(ii), to get back to the prior day's results (e.g., using prior year assumptions and methods). (This adjustment is not required if the unadjusted UVB are higher.) Under the General Rule, contributions made after the premium snapshot date are discounted back to that date at the plan's asset valuation interest rate.

Alternative Calculation Method (ACM): An alternative calculation method is permitted whereby the plan can use the vested CL benefits as required to be reported on the prior year's Schedule B. Add 7% of the non-pay status vested CL liability to account for the accruals in the prior plan year (even if the plan is frozen), adjust the sum by PBGC prescribed methods to reflect the RIR, and bring it forward to the end of the plan year by that rate. The interest rate adjustment is not necessary if the CL rate used in the valuation is less than or the same as the RIR. Large plans with 500 or more participants must adjust their liability figures for significant events between the Schedule B date (first day of prior year) and the premium snapshot date (generally last day of prior year). In the ACM, the RIR is also used in discounting contributions made after the Schedule B date (first day of prior year) back to that date. (The contributions are added to assets as of that date and then are brought forward at the RIR for (generally) one year to the premium snapshot date.) The ACM can produce smaller variable premiums than the General Rule when plan asset returns are poor. Informal PBGC guidance (Q&A 6 of the 2002 Blue Book) provides that a plan need not recognize under "catch-all" significant event 7 (any other event or trend that results in a material increase in the value of UVBs) investment losses that are sustained in the ordinary course of business, provided that the plan's assets are invested in accordance with applicable legal requirements.

When a plan has a short plan year (initial plan year, final plan year due to termination, or changed plan year), the filer may self-prorate the premium (based on the number of full or partial months in the short plan year) and pay only the prorated amount. Note that such proration does not apply where there are short plan years due to a plan going out of PBGC coverage in mid-year or due to mergers, spinoffs, splitups, etc. For purposes of the final plan year due to termination, premiums are payable through the plan year in which assets are distributed pursuant to the plan's termination or in which a trustee (typically PBGC) is appointed under ERISA section 4042. PBGC considers assets distributed if all benefit liabilities through PC6 are satisfied, irrespective of whether residual assets have been allocated yet in accordance with 4044(d).

Mergers, consolidations, spinoffs, splitups, etc., can lead to "duplicate" premiums or to "gaps" in premiums. There is no proration for short plan years to avoid duplication, nor is there any adjustment to avoid gaps. (The PBGC decided to not prorate or otherwise adjust in the interest of simplicity.)

However, as discussed above under "premium snapshot date," in certain circumstances double-counting and non-counting of participants and UVB is minimized or eliminated by shifting the premium snapshot date from the last day of last year to the first day of this year. However, PBGC will not pay refunds or prorate the premium if the plan is amended to create a short plan year and then merges or consolidates (or otherwise ceases its independent existence) at or before the beginning of the new plan year cycle per Instruction B.5.a of the 2005 PBGC premium instructions.

Simplifications:

- Contributions do not have to be added to assets for plans with fewer than 500 participants, since, of course, that can only increase the premium. (PBGC requires larger plans to include contributions because of its need for the information.)
- The premium filer can determine the accrued liability instead of vested liability for plans with 500 or more participants, because that can only increase the premium. Note: It will not increase the premium if the accrued liability is less than plan assets. (Smaller plans can rely on an actuarial certification that there are no UVB to avoid having to provide any asset or liability numbers.)
- The following plans are exempt from determining and paying the variable-rate premium:
    - Section 412(i) insured plans not in arrears (with that status determined as of the premium snapshot date)
    - Plans with no unfunded vested benefits and fewer than 500 participants (this is really just an exemption from reporting, since such plans would owe no variable-rate premium even if the exemption did not exist)
    - Plans with no vested participants (this is also really just an exemption from reporting)
    - Plans terminating in a standard termination with a proposed termination date on or before the premium snapshot date are conditionally exempted from the variable premium for the premium payment year, even though assets have not been distributed. This exemption is conditional upon a successful standard termination.
    - Plans for which contributions were at the §412 Full Funding Limit for the prior year are exempt from the variable-rate premium for the premium payment year. Assets (for purposes of determining the FFL) do not need to be reduced by the credit balance even through §412 would require it. Also note that the interest credit can be added to contributions to see if the §412 FFL is met. This often makes the §412 FFL equal to the §404 deductible FFL. PBGC Technical Update 00-4 explains that the 90% override to the FFL (as added by RPA94) does not require greater contributions for the PBGC FFL exemption than are required for the plan to be at the FFL under Code section 412(c)(7) for funding purposes. Accordingly, a plan qualifies for the PBGC FFL Exemption for a plan year if the sum of contributions to the plan for the prior year (including any interest credited under the funding standard account) and any credit balance in the funding standard account (including interest to the end of the plan year) is not less than the full funding limitation under Code section 412(c)(7). For multiple-employer plans that elected to fund as if separate plans, the FFL criteria is met only if the plan would have met the FFL limit on an aggregate basis, per PBGC Opinion Letter 99-1.

      The FFL exemption had been added by OBRA89, following understandable complaints from plan sponsors and actuaries that they couldn't contribute any additional deductible contributions, but were subject to a PBGC premium for underfunding. However, now that sponsors can deduct up to the Unfunded Current Liability, the FFL exemption no longer makes sense. At the time this Study Note went to press, there were several legislative proposals pending that would eliminate the FFL exemption.

Participant Counts: The PBGC simplified its participant definition (for flat-rate premium purposes) starting with the 2001 premium payment year by moving from a multi-part definition (dealing separately with active, inactive, and deceased participants) to a definition that counts as a participant any individual with respect to whom the plan has benefit liabilities. Under the previous definition, an individual who was earning credited service but who did not yet have any benefit liabilities was counted; under the new definition, such an individual (e.g., new entrant, permanent part-timer) is not counted. An individual is dropped from the participant count in accordance with the following rules. In the case of an individual with no vested accrued benefit, the individual is dropped after incurring a one-year break-in-service under plan terms or after receiving a deemed zero-dollar cash-out under plan terms, or after the individual dies. For a fully or partially vested individual, the individual is dropped after an insurer makes an irrevocable commitment to pay all Benefit Liabilities (BL) with respect to the individual or after all BL are otherwise distributed (e.g., through payment of a lump sum or through the death of the individual without surviving beneficiaries or other continuation of the benefit such as a C&C). Note that a deceased individual with respect to whom the plan has BL counts as one participant, and the beneficiaries (no matter how many) do not count. Also, in a standard termination, an individual who has received a full distribution of BL is no longer counted as a participant, even if the individual is entitled to a share of the residual assets to be paid after the premium snapshot date, per Q&A 5(b) of the 2002 PBGC Blue Book.

Ways to Minimize Premiums

a. Reduce the Participant Count

   (1) Enroll participants on the first day of the plan year or its 6-month anniversary (e.g., January 1 and July 1 for calendar plan years) after reaching age 21 and 1 year of service. This is especially helpful for employers with many young, short service employees and high turnover.
   (2) Use the age 21 and 2 years of service or the age 26 and 1 year of service alternatives in §410(a)(1)(B) if immediate vesting doesn't take away your savings in premiums.
   (3) Deem your non-vested separated employees cashed out (even those that left in the past) and re-file your prior Premium filings for refunds - IRS may only allow a maximum of 2 years retroactive.
   (4) Cash out mandatory ($5,000) and/or voluntary (>$5,000) lump sums, as long as it doesn't cause liquidity problems. However, if lump sums are subsidized, you may find that the premium reduction is less than the subsidy. Also, paying lump sums reduces Funding Ratios that are under 1.0 and could therefore increase your Deficit Reduction Contribution.
   (5) Don't count your transferred employees in each plan - move all their liabilities to their current plan.
   (6) Don't count payee and alternate payee as 2 people.
   (7) Buy irrevocable commitments (annuities) if financially efficient

b. Change your Asset Valuation Method to Market Value if your current method provides a lower asset amount, but remember that you may not be able to switch back easily when you want.

c. Accelerate contributions or reclassify them in prior plan year.

d. If sponsor is close to paying the FFL, pay it.

e. Calculate both the General Rule and ACM premiums and pay the lesser.

f. Improve plan benefits on the first day of the plan year, not right before.

g. Only include vested benefits in current liability - i.e., exclude unpredictable contingent event benefits (e.g., benefits from a possible future shutdown) and non-vested and contingent benefits such as future death and disability benefits, early retirement supplements and subsidies for which employees have not satisfied the eligibility requirements (at least multiplied by the probability that they won't vest). Scheduled benefit increases may be excludable: they are in CL (they are included in 401(a)(2) and must be satisfied before reversion), but are not vested if future service is required to get them.

Due Dates: The variable rate premium and (for plans with fewer than 500 or participants for the plan year preceding the premium payment year) the flat-rate premium is due on the 15th day of the tenth full calendar month following the end of the plan year preceding the premium payment year (October 15 for calendar year plans). For large plans (500 or more participants for the preceding plan year), the flat-rate premium is due on the last day of the second full calendar month following the end of the prior plan year (February 28 or 29 for calendar year plans). To avoid penalties (not interest), the participant count must be at least the lesser of 90% of the current year's count or 100% of the count on the prior year's premium filing. This early filing is generally done on an estimated basis, with a reconciliation payment due at the same time the variable-rate premium is due.

3. Multiemployer Plans

The multiemployer fund is in better shape than the single-employer fund, and guarantee levels are much lower than they are for single-employer plans. As a result, the multiemployer premium is only $2.60 per participant (using the same definition of participant as is used for single-employer plans). There is no variable rate premium. The premium due dates are the same as the due dates for the flat $19 portion of the premium for single-employer plans.

4. Premium Audits

The PBGC has been increasing the number of its audits of premium filings. Although the audits have focused primarily on flat-rate premiums in the past, they are focusing more on variable-rate premiums. In many cases, the audits start with sampling techniques to determine whether the PBGC should conduct a more in-depth audit. It is important to keep records for six years to support the premium determinations in the event of audit. A recent sample PBGC Premium Audit is in Appendix B.

5. Penalties for Late Premiums

In addition to late payment interest charges (based on interest rates in IRC § 6601(a), PBGC charges a penalty of 1% per month or 5% per month, up to a maximum of 100% of the unpaid premium (per PBGC regulation §4007.8). The 1% rate applies to the portion of the late premium that was paid on or before the date the PBGC issues a notice that there is or may be a premium delinquency (including a letter initiating an audit), and the 5% rate applies to the portion paid after that date. Requests for reconsideration of a penalty determination can be filed up to 30 calendar days after being notified of the penalty assessment.

III. EVALUATING AND IMPLEMENTING A PLAN TERMINATION

1. Evaluating a Plan Termination

Who Is Involved? In a voluntary termination, the first question is- who is involved in the decision to terminate? Per §4041(a)(1), (b)(1)(A), and (c)(1)(A), the Plan Administrator (or the PBGC) is needed to terminate a plan. However, all contributing sponsors and their controlled groups are involved since they can be affected (through PBGC's joint and several liability claims under §4062). Will a collective bargaining agreement be violated? If a union submits a formal challenge to the termination, PBGC cannot proceed due to the provisions of regulations §4041.7. The PBGC must suspend the termination process pending resolution of the challenge. You may want to have discussions with the union up front. (It has been easier to reduce or eliminate retiree health benefits to retired salaried workers than to hourly retirees who could look to the union's bargained contracts.) Do implicit agreements with employees through employee benefit booklets or other representations or promises require the maintenance of a plan? Therefore, the collective bargaining agreement, the entire plan, the SPD, and all related benefits documents should be read.

Can you terminate? This will depend on whichever document is most generous to the participants, as the courts often favor participants. Many plan sponsors insure that plan documents and summary plan descriptions (SPD) state that benefit accruals may be frozen, the plan may be terminated, and assets reverted. If the plan document is more generous to participants than the SPD then courts will follow it (especially if the SPD contains a disclaimer that the plan document prevails in the case of any misstatement or omission in the SPD). On the other hand, sometimes a more generous SPD may affect the outcome of a plan termination dispute, as in the denial of an asset reversion. Courts have allowed companies to terminate their retiree health plans if both the plan documents and SPD call for it. The point is that a lawyer should review all relevant plan documents, SPD, bargaining agreements, web sites, workbooks, and other written communications to be sure there will be no legal obstacles to terminating the plan.

Who decides? It is important that the authority to amend or terminate a plan is clear in the written document controlling the plan. There have been court cases for retiree medical plans and severance plans where the plan documents did not clearly state the procedures for terminating the plans, or there was no written action by the proper authority to terminate the plan. Thus, the plans either could not be terminated, or they were not terminated when management thought they were. Most pension plans are clear about who can terminate them (usually the Board), but these cases suggest nothing should be taken for granted. When management intends to curtail or terminate any employee benefit plan, these cases suggest we list all plans and have the appropriate authority to take the necessary action to curtail or terminate them (and so notify employees.)

Why Terminate? Terminations can result from corporate mergers and acquisitions, a desire for the surplus assets, needs to reduce costs, cessation of business operations, the divestiture or breakup of (formerly) one employer, or just frustration with constantly-changing, complex laws and regulations. Converting a plan from a Title IV covered plan to a non-covered plan (e.g., converting a DB plan into a DC plan) is also a termination. When converting from a DB plan to a DC plan, many provisions of the DB plan must be preserved unless:

(1) the transfer is elected by the employee,
(2) notices and spousal consent rules are followed,
(3) an immediate benefit is available, and
(4) an actuarial equivalent benefit is offered (See 1.411(d)-4,Q&A3).

These conversions must follow Standard Termination rules also.

Some plans paid out lump sums to all non-substantial owners. This results in a loss of PBGC coverage, but is not a plan termination per PBGC Opinion Letter 90-6 www.pbgc.gov/docs/OpLtr595.htm

Indirect adverse consequences of terminations are possible, such as the following:

- The IRS could determine that the plan was not adopted as a permanent program - just a tax deferral ruse for owners. They will want to know if the termination of the plan was for a valid business reason.
- Remaining plans whose qualification depended on the terminated plan's existence (say, for non-discrimination purposes) would lose their qualification.
- Asset reversions will be subject to income and excise taxes.
- Assets (e.g., Real Estate) may not be easy to liquidate. Some employees may want to keep their insurance policies.

FAS 88 & FAS 132 should be reviewed to see how the company's financial books will be affected by this settlement of liabilities.

Frozen Plans and Wasting Trusts: Terminating a plan can be a very difficult and/or costly task; simply freezing accrued benefits may be preferred (as long as this does not create §401(a)(26) problems). Freezing plans could also cause coverage and §401(a) qualification problems down the road. For example, non-highly compensated employees (non-HCEs) may terminate faster than HCEs, and cause coverage problems. Wasting trusts (frozen plans with no real plan administrator or contributing sponsor) are discouraged by the IRS. Regulation 1.401-1(a)(2) suggests that, with a wasting trust, an essential element of that plan's qualification would be lost (i.e. there is no longer an employer maintaining the plan). Who would amend the plan to keep it qualified when laws were changed? Who would do the 5500 filing?

Partial terminations can result from a cutback in accrued benefits or a substantial reduction (e.g. 20%) in the number of active employees caused by the employer (e.g. a layoff). These are called horizontal and vertical partial terminations, respectively. A partial termination is primarily a plan qualification concept, and is not subject to the plan termination procedures described later in this chapter because it is not an actual plan termination. Non-vested benefits become fully vested to the extent funded under §411(d)(3). In one partial termination, over 6,000 non-vested Gulf participants claimed they were owed some of the plan's surplus (in addition to the full vesting of their benefits which they did get). The Fifth Circuit in Borst v. Chevron Corp. (the buyer) 1994 US App LEXIS 29473 disagreed and said that §4044 requires allocation of excess assets only upon full (not partial) plan termination. It also found that the plan did not call for any reversion to the participants. Non-vested benefits may also vest upon the suspension or cessation of contributions in a Profit Sharing or DC plan. In those plans, whether a plan has terminated depends on the facts and circumstances. The Court of Appeals for the Second Circuit in Weil v. Retirement Committee of Terson Co. ruled that the percentage reduction in only non-vested employees was the determining factor regarding whether a partial termination occurred, but the IRS in a private letter ruling said both vesteds and non-vesteds should be counted in the fraction.

Defining "termination" can be tricky. Under §411, the IRS is quicker to suggest that a termination has occurred (for purposes of vesting affected employees) than under §416, where the IRS will suggest that a termination has not occurred (and therefore top-heavy accruals will continue) unless the plan's assets are distributed "as soon as administratively feasible" as discussed in Revenue Ruling 89-87. This is one reason why the IRS and PBGC push quick deadlines and prefer not to allow the uncertain status of frozen plans or wasting trusts to continue indefinitely. It also delays the IRS's receipt of the reversion excise tax and income tax.

The effect on employees should also be considered. How will plan termination affect employee morale, hiring, and retention? The lack of an adequate pension plan will complicate the task of managing an

orderly retirement of employees at appropriate ages, could lead to age discrimination claims, and force embarrassed employers into messy, pay-as-you-go retirement arrangements. Thus, before implementing a plan termination, the pension consultant should ensure the company's board has made an informed decision to proceed.

Involuntary Termination: A plan termination may also happen involuntarily. Under §4042, the PBGC may terminate a plan if:

(a) The plan has not met the minimum funding standards of IRC §412;
(b) The plan will be unable to pay benefits someday;
(c) A distribution of $10,000 or more to a substantial owner has left plan underfunded; or
(d) The possible long-run loss of the corporation with respect to the plan may reasonably be expected to increase unreasonably if the plan is not terminated.

The PBGC, in conjunction with the courts or by agreement with the plan sponsor, can choose a retroactive date. In addition, an involuntary termination can proceed notwithstanding a challenge from a collective bargaining unit, whereas Standard and Distress Terminations can be delayed. The PBGC sometimes threatens involuntary terminations before the spin-off of a plan to a weak buyer or before wealth leaves a Controlled Group that maintains an underfunded plan (such as wealth leaving through the sale of a profitable subsidiary).

Mandatory Termination: If the plan is running out of assets to pay benefits that are currently due, then the PBGC must take over the plan, per Section 4042(a) second paragraph. This was a method used in the past to get the PBGC to pay benefits. A sponsor would just annuitize or lump out enough participants to use up the assets. Then the PBGC had to take over the plan immediately. RPA94 made this harder with the solvency funding in §412(m) rule which says a plan cannot pay out annuities or lump sums beyond the point where plan assets would be less than 3 years worth of benefits. In addition, sponsors need have been sued by the remaining employees in the plan for doing this, because the participants remaining in the plan will only get their guaranteed benefits, which may be less than their full accrued benefits.

2. Implementing a Plan Termination

Except for Involuntary Terminations instituted by the PBGC under §4042, a plan administrator may initiate a termination of a covered plan in only one of two ways per §4041(a)(1) - Standard or Distress. Under a Standard Termination the assets of the plan must be sufficient for all "benefit liabilities" determined under IRC §401(a)(2). (See Chapter VII, Section 9 for more details on what is included in all "benefit liabilities".) If assets are not sufficient, the sponsors must qualify under the tighter rules for a Distress Termination (all sponsors and each member of their controlled groups must be in serious financial difficulty).

The following pages give a step-by-step process on how to terminate a Pension Plan. They reflect the final PBGC Regulations 4041 and the filing forms issued for use through September 30, 2007. It should be noted here that ERISA §4071 authorizes the PBGC to assess penalties of up to $1,000 per day when notices are late (increased for inflation to $1,100 at this writing). The PBGC penalty policy generally provides lower penalties of $25 per day for the first 90 days and $50 per day thereafter, with lower penalties for small plans. Deadlines can be found in regulations 4041, the Instructions to PBGC termination Forms 500 and 600, and on the following pages.

Standard Termination Checklist

1) Board action to implement termination. Action should address termination and final qualification amendments. Separate action should be taken to freeze plan and limit non-protected benefits, in case there is a problem with the termination.
2) NOIT to affected parties - at least 60 days in advance of proposed DOPT (but not more than 90 days). Tell participants: PBGC's guarantees are extinguished by lump sums and annuities. The 204(h) notice may be combined with the NOIT mailing, but will generally be on separate pages.
3) If not combined with NOIT, prepare and distribute 204(h) notice.
4) After NOIT, no distributions such as lump sums or purchased annuities (unless such transactions are consistent with past practice and as long as sufficiency is not jeopardized) until end of PBGC review period. §4041.22
5) Begin diligent search for missing participants. Use NOIT and 204(h) notice returns to begin list of the missing. Hire outside search services, if necessary.
6) Develop and implement a revised investment strategy consistent with interest-sensitive liabilities and need for cash available to settle the liabilities within the next twelve months.
7) Freeze accruals and remove by plan amendment certain death & disability benefits which are not protected by the anti-cutback rule in §411(d)(6). Deem non-vested separated employees cashed out. If the plan does not currently provide lump sums, amend the plan to allow paying minimum lump sums, comply with all laws on DOPT, allow payment of expenses from plan (if very over funded), reduce reversion through non-discriminatory benefit improvements. Adopt them on or before DOPT, since post-termination amendments decreasing benefits may not be allowed.
8) Post Notice to Interested Parties to announce that plan will be submitted to IRS. Request determination letter using IRS forms 5310 and 6088. Pay user fee with Form 8717.
9) Notice of Plan Benefits to participants and beneficiaries no later than item (12). Now may be a good time to confirm information for IRS Form 6088 and to send REA election plus §402(f) and IRS Announcement 8702 tax information, but remember that elections must be within 90 days of distribution per §1.417(e)-1(b)(3).
10) Is Contributing Sponsor's Agreement to make Plan Sufficient needed? See §4041.21(b)(1)
11) Would an alternate treatment (similar to a waiver) of Majority Owner's benefit help? See §4041.21(b)(2).
12) Standard Termination Notice to PBGC using Forms 500 and EA-S filed with PBGC within 180 days after proposed DOPT. The proposed DOPT can be moved up to 90 days after NOIT. Assets must equal or exceed liabilities based on an estimated insurance company bid plus lump sum amounts. If necessary, sponsor must execute commitment to make the plan sufficient before the actuary signs Schedule EA-S. This step must not happen before the Notice of Plan Benefits is distributed, and should not happen before the 5310 is filed (to avoid timing problems at the end of the process). Note questions regarding compliance with on 5-year rule for amendments increasing reversion and Joint Implementation Guidelines (reversions within 3 years of a spin-off or termination-reestablishment).
13) A challenge from collective bargaining units stops the clock. §4041.7
14) PBGC Review: Hopefully, no letter of Non-compliance will be issued by PBGC within the 60-day review period. If a Notice of Non-compliance is inconsistent with participant interests, the PBGC does not have to nullify a Standard Termination due to failure to comply with the requirements in law.
15) IRS issues favorable determination letter.

16) Get Insurance Company bids on irrevocable commitments preserving all benefits, forms, options (including lump sums), rights, and consent requirements. §4041.27(d)(1)

17) Fiduciary decisions: choice of insurance company, plan interpretation, lump sum calculation, etc. Be sure to follow DOL guidelines regarding documentation of the selection process. The fiduciaries must choose from among the safest available insurance companies. If statement of insurers was not part of the NOIT, distribute supplemental annuity notice to the PBGC and all affected parties (e.g., participants) entitled to benefits (other than those who will receive mandatory cashouts) that, in addition to other information, discloses the names of the insurance companies from among whom annuities will be purchased. The addition of a new insurer requires a new supplemental notice. The last supplemental notice must be issued at least 45 days before distribution.

18) Distribute payment election forms, QJSA notices, and tax notices to participants eligible to make payment elections. Obtain written payment elections (including spousal consents, if necessary) from participants.

19) Employer must contribute the amount, if any to the plan necessary to pay all plan benefits.

20) If assets are still sufficient, purchase annuities and make lump sum payments to participants and beneficiaries. This all must occur within 180 days after the PBGC review period or 120 days after receipt of a favorable IRS determination letter, if it was filed timely (on or before the date the Standard Termination Notice filed with PBGC). Request PBGC to extend time to distribute assets (if necessary) "for compelling reasons" at least 15 days before the normal deadline for this step. Notify participants when obligation rests with insurer within 30 days of a copy of the contract or a certificate being available.

21) The PBGC will handle missing participants if P/A cannot find them after a diligent search and if PBGC is paid:
(a) the plan's lump sum amount (if # $5,000) or
(b) the PBGC PV (if > $5,000) but not less than the plan's lump sum amount

22) Post-Distribution Certification (PBGC Form 501) must be received by PBGC within 30 days after distribution date (daily penalty starts accruing 90 days after the distribution deadline). PBGC premiums accrue until Certification filed. Plan Administrator must retain employee and plan data and calculations for 6 years.

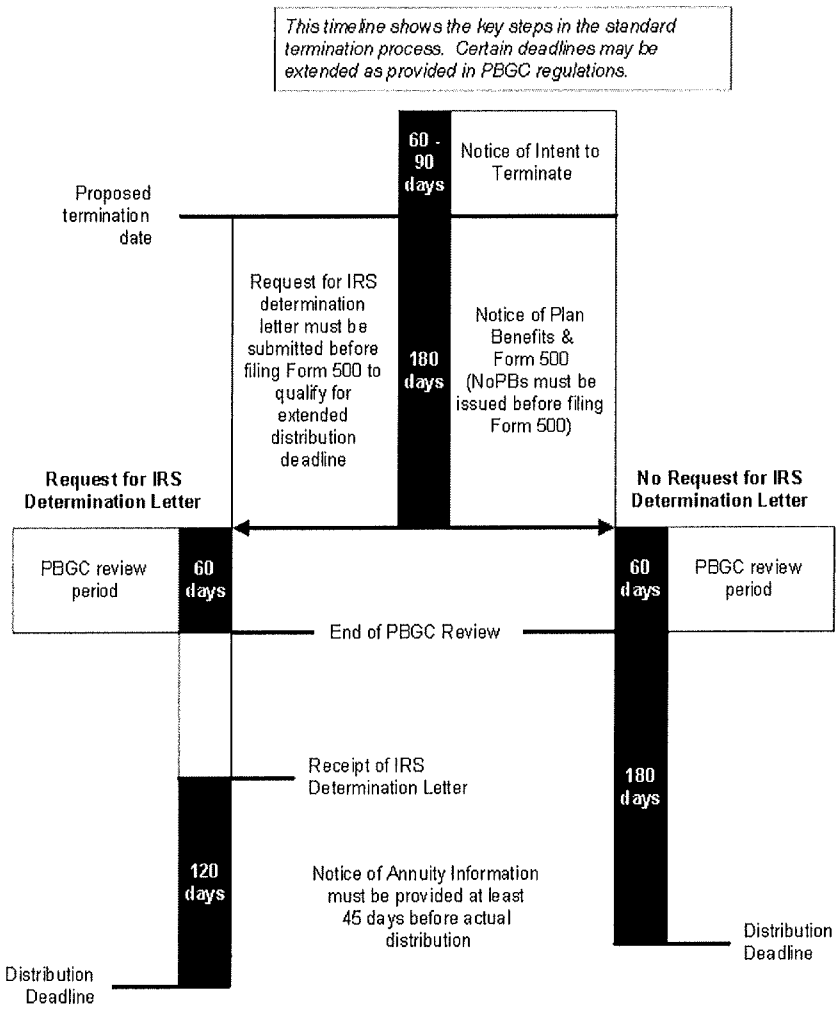
23) Pay asset reversion (if any) to employer.

24) Pay excise tax (Form 5330) on last day of following month and Income Tax on total reversion.

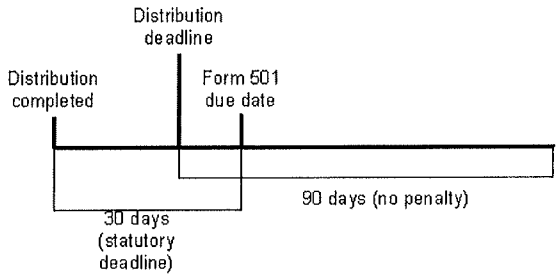
25) Complete final Forms 5500 and PBGC-1 (or successor premium filing form or procedure). The last plan year ends upon satisfaction of all benefit liabilities for premium filing purposes, and ends upon complete distribution of all plan assets for Form 5500 filing purposes. Due dates for the forms are calculated from these respective dates, not from the end of the traditional plan year.

26) The PBGC audits virtually all plan terminations with 500 or more participants, and a statistically valid sample of other terminations, to ensure that participants and beneficiaries received correct amounts and that consent rules were followed, etc. It is good practice to compile an "audit file" during the course of the plan termination process, so the material is readily at hand when the audit materializes.

Standard Termination Timeline:
Notice of Intent to Terminate to Distribution Deadline



Standard Termination Timeline:
Post-Distribution Certification



Source: PBGC Instructions to Form 500.

a. Standard Terminations-Assets Sufficient for all Benefit Liabilities ERISA Section 4041(b) and PBGC Regulation 4041 Subpart B

(1) Board Decision: Before implementing a Standard Termination, the pension consultant should ensure the company's board has made the decision to proceed. A board resolution that the plan be amended to meet all requirements for qualification is helpful. It ensures that your adopted date is pre-DOPT, even if you forget some provisions. Action should address termination and final qualification amendments. Separate action should be taken to freeze plan and limit non-protected benefits, in case there is a problem with the termination. Note that while amendments to ensure plan qualification can be made after the termination date, any discretionary choices within the qualification rules must be made and incorporated into the plan before the DOPT.

(2) Notice of Intent to Terminate (NOIT) - §4041.23

The plan administrator should notify all affected parties of its intent to terminate at least 60 days (but not more than 90 days) prior to the proposed date of plan termination (DOPT).

"**Affected party**" (§4001.2) means each active participant, each deferred vested participant (including non-vested separated employees to the extent required by the IRS), each retiree, each beneficiary of a deceased participant, each alternate payee under a qualified domestic relations order (QDRO), each union representing plan participants (including unions decertified in the last 5 years if there is no current union), and any person designated in writing to receive notice on behalf of an affected party. If some affected parties were discovered after the NOIT goes out, the termination will not fail as long as Notice is sent as soon as the parties are found - per 4041.3(c)(3). The NOIT can help determine who is missing up front. Note that while the PBGC is an "affected party" for Standard Terminations it need not get the NOIT. In the case of a spin-off/termination transaction, affected parties include the participants in the ongoing portion of the plan that is not terminating. The Plan Administrator must provide a notice describing the transaction to them.

Timing: Make sure the notice is at least 60 days before DOPT (i.e. if the notice is sent out on day 1, the DOPT can not be before day 61) but not more than 90 days earlier. A common error with a NOIT is that they are not sent out early enough since people often forget February has less than 30 days.

Contents of the NOIT are set forth at §4041.23(b). Merely telling employees that the employer is going to stop contributing is not acceptable. The Notice must clearly say the plan will terminate in a Standard Termination, that accruals will stop, that assets are sufficient, and give the proposed DOPT. The Plan Administrator (P/A) must also inform participants that distribution of annuities and lump sums will extinguish PBGC's guarantees - and, if known, the name of the insurer that will be used (so that employees can complain if they think the insurer is weak), a description of state insurance guaranty arrangements, and an explanation of what happens to the accruals if the termination fails. PBGC provides a sample NOIT with a description of the state insurance guaranty arrangements. See PBGC regulation 4041.23(b)(5) and 4041.27. The P/A should describe the effects of cessation of benefit accruals, and how to obtain an SPD. If the insurers from among whom annuities will be purchased are not known at this time, the P/A should state that this information will be provided at a later date, but in no event later than 45 days before the distribution date. The notice will contain information identifying the plan and the sponsor by name and identifying numbers, and the notice will provide contact information about the person responsible for answering questions about the plan termination.

Court Cases: According to Addison v. United Air Lines, Inc. (N.D. Ill. 1988), an employer may decide to withdraw a Notice Of Intent to Terminate so that the plan may continue to be in effect, even after the

PBGC has approved the termination. (The employees sued because they were looking forward to a lump-sum.) In American Flint Glass Workers Union v. Beaumont Glass Co. (1995, CA3) 1995 US App LEXIS 21650, the Third Circuit had a similar decision when the employer decided to halt the Plan Termination. The employer found the plan was quite underfunded and they were not ready to contribute enough to make the plan sufficient. The Court in Payonk v. HMW Indust., Inc., 883 F.2d 221 (3rd Cir. 1989), held that the termination notice requirement does not create a fiduciary obligation to give plan participants notice of earlier discussions concerning termination. In this case, plan participants who terminated before the NOIT felt they deserved some of the surplus assets because they were not notified of the contemplated termination decision. The court held that the employer did not have a fiduciary duty to give participants earlier notice of the termination. Other court cases have gone in both directions about whether employees should be notified of early retirement windows that may open up in the future. The court decisions generally uphold a plan administrator giving out honest information that it is unclear at this point whether there will be an early retirement window. More details on this can be found in the fiduciary section of this Chapter.

Another court case illustrates the legal responsibilities that the NOIT and other plan termination notices may create for the plan actuary. PBGC v. Beadle, 9 EBC 1809 (E.D. Mich. 1988), held that the PBGC may sue an actuarial firm for breach of its professional obligations and for any adverse effects on a plan's insufficiency due to the actuarial firm's failure to file a NOIT for a pension plan. The PBGC alleged that the plan sponsor directed the actuarial firm to file the notice with the PBGC. The actuarial firm was not being paid, but never told the plan sponsor in writing that it had not filed the notice. The case was eventually dismissed.

The 204(h) notice (see below) may be combined with the NOIT mailing, but will generally be on separate pages.

(3) Distribute 204(h) notice. If not combined with NOIT, prepare and distribute ERISA 204(h) notice. On April 9, 2003, the IRS issued final regulations (Section 54.4980F-1) providing guidance on the notification requirements under section 4980F of the Internal Revenue Code (Code) and section 204(h) of ERISA. Generally, the regulations provide that an amendment ceasing benefit accruals on a future date, even if it is the plan termination date, is subject to the requirements of 204(h). The example in Q&A 17 provided example language stating that the benefit accruals would cease on the specified future date "whether or not the plan is terminated on that date." Such language is much safer than saying accruals will cease "on the termination date," because if there is a problem with the termination date, benefit accruals will continue until the termination date, regardless of the language in the plan amendment. In any event, 204(h) cannot require benefit accruals beyond the plan termination date. As noted in Step 1, it is best to take separate actions to freeze the plan and to terminate the plan.

The general rule is the 204(h) notice must be provided at least 45 days before the reduction in benefit accruals. This rule is satisfied if the notice is provided with the NOIT, unless the accruals will be stopped before the date of plan termination. In that case, the 204(h) notice must be provided in a timely fashion relative to the cessation of benefit accruals.

The notice itself should not be difficult to write. In the regulations, there is an example of a plan that ceases all benefit accruals. The plan administrator simply describes the current plan formula, states that as of the given date, no participant will earn any further accruals, and states the effective date of the amendment. This simple statement is deemed to comply with the requirements of 204(h). See the regulations for more details.

(4) Restrict Lump Sum Distributions and Irrevocable Commitments (§4041.22): After NOIT, no distributions such as lump sums or annuities until end of PBGC's 60-day review period (unless consistent with past practice and as long as sufficiency is not jeopardized).

The PBGC is concerned because if the plan becomes an insufficient Distress Termination, it will be difficult for the PBGC to reclaim those lump sum and annuity distributions from participants and Insurance Companies. Some Insurance Companies may allow a revocation of the annuity contract if the termination fails. This could be very valuable. There is also concern if lots of partially vested participants are cashed out pre-DOPT in order to avoid becoming fully vested on DOPT.

(5) Initiate Missing Participant Search. Begin diligent search for missing participants. Use NOIT and 204(h) notice returns to begin list of the missing. Hire outside search services, if necessary. If the sponsor has a good handle on who is missing, the search can begin up to six months before the NOIT is issued.

(6) Assets: Determine your liquidity needs and immunize. The investment managers should be informed that the plan might terminate, in case it is desirable to move toward liquid investments. For example, should the plan's real estate investments be sold?

If your assets barely cover liabilities, bonds with durations similar to those of your liabilities are helpful. If interest rates decline (causing annuity purchase rates and possibly plan lump sum amounts to increase), it would be helpful if assets went up by approximately the same amount. The actuary can offer to provide the money manager with cash flows or duration estimates for participant classes (active, retired, deferred vested, etc.) or other calculations that might be useful in setting a revised investment policy. However, if the plan always determines lump sums using an interest rate of 5% (or the GATT rate if lower), then you won't want assets to swing in value if interest rates change above 5% (at least for the portion of participants that are expected to choose lump sums).

(7) Amend Plan: Plans do not need to be amended to terminate the plan per Aldridge v. Lily-Tulip, Inc. Salary Retirement Plan Benefits Committee (1994, CA11) 1994 US App LEXIS 36300. The 11th Circuit noted that the plan termination had Board approval and a §4041 procedure (including an NOIT to employees). The Supreme Court declined to review the case (US Sup Ct, No. 95-526, 9/28/95).

However, most practitioners recommend the following amendments to be safe. **Freezing accruals and participation** should be considered in case the IRS or PBGC does not approve the termination as desired. Remember that top-heavy plans may not be able to cease accruals for certain employees (see 1.416-1,T-5). One should also consider **amendments removing unprotected benefits** such as death and disability that are not protected by the anti-cutback rule in IRC §411(d)(6). Otherwise, the plan sponsor may have to include these benefits in the insurance contracts post-DOPT. Be careful that you are not breaking any plan provisions or statements in an SPD. You may want to amend the plan to **allow lump sums** and to mandate lump sums without consent if $5,000 or less. It helps if you put into the plan document that "non-vested separated employees are **deemed cashed out** and thereby forfeit all rights under the plan". This may only be used retroactively for separations in the last two years per Revenue Ruling. If the plan is over funded, be sure the plan provides for the payment of expenses. You may also wish to provide nondiscriminatory benefit improvements in order to minimize a reversion of funds to the employer and the resulting excise taxes.

Amend the plan to **comply with all laws** in effect on DOPT. A board resolution that the plan be amended to meet all requirements for qualification is helpful. It ensures that your adopted date is pre-

DOPT, even if you forget some provisions. PBGC regulation 4041.8 states that **post-termination amendments** will be disregarded to the extent they hurt participants (e.g., decrease benefits or eliminate or restrict options), unless required to meet qualification requirements or an individual's residual assets are used to increase his/her benefits. Remember that decisions on qualification rules that allow choices must be incorporated into the document before the plan termination date.

(8) Request a Determination Letter From IRS: In order to ensure that you have followed the IRC and not done anything to harm the qualification of the plan, submit the plan termination to the IRS on Forms 5310 and 6088 for a determination letter. Also, submit Form 8717 with your user fee. Forms can be procured by calling 1-800-829-3676 or accessing www.irs.gov/formspubs/index.html .

Content: Some questions on the Form 5310 determine whether a significant percent of participants left the plan (if they left at the initiative of the employer, then a partial termination might vest more participants) and whether an amendment decreased benefits (if it was in the past 5 years it may have increased the reversion which would violate 4044(d)(2)). The 5310 also asks if there is a business necessity for the termination because qualified pension plans are supposed to be permanent. Form 6088 tests whether there is discrimination in favor of the top 25. The form is simpler now since it no longer is interested in key employees (just HCE's - highly compensated employees defined at §414(q)) and only 5 years (not 10 years) of historic compensation is needed. Total compensation should include §401(k) deferrals. The plan may have to undergo the average benefits test or non-discrimination-in-amount test unless it received a favorable determination letter within the last 3 years stating that the average benefits test or non-discrimination general test or safe harbors were met. If a material change in facts (e.g., increasing benefits pro-rata to use up surplus) occurred since the determination, the plan will have to submit a general test again.

Required? Although helpful, requests for an IRS determination letter are not required, and some plans have skipped this step. The actuary may want to be on record (and in writing) recommending the client file for a determination letter. Form 5500 asks terminating plans if they requested a determination letter. If not, there is a high probability of audit. The IRS wants to ensure that the plan was amended for recent tax law changes. The PBGC also sends the IRS a list of terminating plans that are getting a reversion.

Reasons for requesting a determination letter are:

1. A favorable determination letter issued upon termination expresses the IRS's formal opinion that the termination does not adversely affect the plan's qualification status.

2. The IRS generally cannot retroactively change its determination unless the application misstates or omits material facts, or the facts as subsequently developed in the termination are materially different from the facts on which the determination letter was based.

3. It's better to know in advance which plan provisions need fixing because if a plan becomes disqualified upon termination, it would create taxable income for plan participants, and conceivably, liability on the part of the plan administrator or sponsor to such participants.

4. Some banks may want to see a determination letter before they distribute assets.

5. Filing a timely determination request may give you more time to distribute assets. See section on Final Distributions, later in this Chapter.

Timing: A notice to interested parties must be distributed within the usual time frame (participants should see it approximately 1 to 3 weeks in advance of the 5310 filing) to the same people as the NOIT, except it need not go to beneficiaries and former unions. See Revenue Procedure 2005-6 or its successor for an update on these rules. (The plan administrator may also want to send something that can be understood by employees.) As the PBGC requires distribution as soon as practicable, it is advisable to submit application for qualification to the IRS early, due to the longer delays likely in receiving the IRS determination letter and their conflicts with the PBGC. If one files their request with the IRS on or before the date they file the Standard Termination Notice, then distribution can be delayed until 120 days after a favorable determination is received per the PBGC's Form 500 instructions.

The frequent passage of new legislation often means plan documents are not up to date with the latest rules and regulations even if the plans have been operationally in compliance with the recent laws. When the plan is terminated, the IRS will usually expect the plan to be brought completely up to date to the extent possible as of the DOPT.

Some information on Forms 5310 and 6088 is the same as information contained in the Notice of Plan Benefits (see below). Calculating the exact benefit amounts for the Notice of Plan Benefits takes time and careful review. Some actuaries go ahead and file the 5310 and 6088 with estimated amounts in order to get the filing in the IRS queue as soon as possible. When the Notices of Plan Benefits are ready, an updated 6088 can be submitted to the IRS reviewer. This strategy can help expedite the completion of the determination letter process.

(9) Notice of Plan Benefits (NOPB) - §4041.24: - must be sent to participants and beneficiaries on or before the date Standard Termination Notice is filed with the PBGC (which must be filed no later than 180 days after the proposed DOPT), per §4041.24(a).

Contents include the DOPT, estimated benefit amounts (at earliest and normal retirement dates) and forms, information on the employee data used to calculate benefits, and the availability of other options in language that can be understood by the recipients. The notice should contain a statement urging the affected party to notify the plan administrator of any errors in the employee information used to calculate benefits. The effect of interest rates on lump sums must be provided to those that might get lump sums. Regulation 4041.24 details what information is needed and whether the notice must be printed in a foreign language. It reduces the required information for retirees, terminated employees, those who are getting a mandatory cash out, and those who have elected their benefit.

Participants deserving of a Notice may include certain non-vested separated employees if they are entitled to benefits based on IRS's interpretation of 411(d)(3). Read this Study Note's discussion of PC6 (Priority Category 6) in Chapter VII for more details. Missed participants must get their Notice when discovered. In spin-off/terminations, notices must be issued to all participants in the ongoing plan also.

The notice may provide a good vehicle to find inactive participants, send out REA elections and withholding forms, and to inform employees of tax consequences of benefit distribution as required by IRC 402(f). Also review IRS Announcement 87-2 or its successor for a summary of tax items to be given to participants. In many cases, especially for larger plans, the timing may not work out. In this case, the elections may have to be provided later (within 90 days of distribution per 1.417(e)-1(b)(3)). The feedback from this notice may provide information helpful to the filing or updating of Form 6088 with the IRS in the previous step (#8), so if possible, send the notice out as early as possible, so that you can still get this and the IRS forms filed before the Notice to the PBGC, which has a time deadline (see #12).

(10) Commitment to Make Plan Sufficient - §4041.21(b)(1)

A plan sponsor may contribute whatever assets are needed to make the plan sufficient for all benefit liabilities. For Standard Terminations, IRC §404(g) (and 1.404(g)-1) allows a deduction only through PC4's guaranteed benefits. Additional deductions under §404(a)(1)(A)(iii) can be carried over into the next 10 tax years ratably per 1.404(a)-6(b)(3). OBRA87 reduced this problem for single employer plans with more than 100 employees (counting employees in all DB plans of the employer and its controlled group on at least one day of the previous plan year, but excluding employees not in the CG or not in a DB plan). Per §404(a)(1)(D), it allows a deduction for amounts up to the Unfunded Current Liability (UCL) for such plans. This section was further modified by adding §404(a)(1)(D)(iv) that provides an exception to deduction limits in *the year the plan terminates only*: Substitute the amount required to make the plan sufficient for benefit liabilities for the Unfunded Current Liability limitation mentioned above. This will require the determination of these liabilities and the amount necessary to fund them no later than 8 ½ months after the end of the plan year in which the plan terminates. This may argue for scheduling your termination date at the beginning of a plan year instead of at the end of the year to give yourself twelve additional months to determine benefit liabilities for tax deduction purposes. Other ways to increase contributions so that you can terminate the plan as soon as possible are:
(a) Use the lowest interest rate within the corridor to get the largest deduction.
(b) use a strong mortality table with generational mortality improvements,
(c) use conservative, but reasonable, assumptions, such as an expense loading if you are buying annuities, subsidized lump sums (to the extent they will be utilized),
(d) reflect early retirement subsidies with early retirement assumptions (to the extent they may be used),
(e) a stronger actuarial method (aggregate?).

If you have to contribute more to make the plan sufficient, then there still may be deduction problems and thus a §4972 10% excise tax. However, an IRS General Information Response (in Appendix B) said that the §4972 10% excise tax (on amounts contributed to the plan which are not deducted yet) does not apply after a plan terminates, since there is no longer a "qualified employer plan" as defined by §4972(d)(1). It might apply in the first year though (i.e., the year the plan terminated). Effective for tax years ending on or after 12/8/94, RPA removes the *excise tax* on terminating plans with 100 or less participants but only on contributions up to the UCL. (There is still the *deduction problem* however on amounts above and below the UCL.) Other techniques discussed at the 1994 EA meeting were to pay participants with benefits beyond PC4 (see Chapter VII) with the assets available, switch to end of year valuations, and then determine your deduction.

Current Liability (CL) is defined in the law at Code Section 412(l)(7). The interest rate must be consistent with current insurance company purchase rates and be within the 90% to 105% corridor permitted by 412(b)(5)(B) and the mortality table must be 83GAM (M,F) per Rev. Rul. 95-28. Some year after 1999, Secretary of Treasury must propose a new table that reflects pensioner mortality and future mortality improvement. Current Liability includes all liabilities under 401(a)(2) determined as if the plan had terminated (which would include contingent benefits and scheduled benefit increases, if the contingency is satisfies by future service). Conference Committee Reports for PPA Section 9303 state that CL includes early retirement subsidies, social security supplements, and survivor subsidies. The Reports hint that the portion of contingent benefits earned to date could be valued using withdrawal rates. The IRS has not yet decided whether to limit it to just (a) §411(d)(6) protected benefits plus something for the contingent benefits or (b) all benefits. However, CL expressly does not include unpredictable contingent benefits (e.g. certain shutdown benefits) per 412(l)(7)(B) unless the event has already occurred. IRS Notice 90-11 says that subsidies in benefits such as subsidized lump sums can not be reflected in Current Liability because otherwise one could get around the Current Liability interest rate by

using the plan's lump sum interest rate which might be below the permissible corridor. IRS made an "exception" so that subsidies in non-decreasing life annuities can be included in Current Liability. Bills before Congress now will require that Lump Sum amounts be included to the extend they are elected.

The interest corridor causes a deduction problem. Some practitioners have suggested that you could distribute to the people with subsidized lump sums and then perform an end-of-year valuation, and deduct up to the full UCL.**DB/DC:** Sponsors who fund both DB and DC plans will have to be careful with the 25% of the compensation limit in §404(a)(7) (where maximum includable pay is $150,000 (with indexation)). If the employer wants to contribute and deduct an unfunded CL amount which is over 25% of compensation, then no contribution can be made to the DC plan. Effective for tax years ending on or after 12/31/92, RPA eliminates the excise tax for plans with over 100 participants that contribute the UCL to the DB plan and 6% of compensation to a DC plan, even though they total more than 25% of compensation. This did not fix the deduction problem, however.

A sample contributing sponsor's "Agreement for Commitment to Make Plan Sufficient for Benefit Liabilities" was in the Appendix to the proposed PBGC Regulation 4041. The requirements for the commitment are found in final regulations 4041.21(b). The actuary should require such written commitment to the plan from the sponsor and be satisfied that such commitment can be met. The value of such commitment should be included in plan assets on Schedule EA-S (but the PBGC does not want a copy of the Agreement).

(11) Waivers of Benefits - §4041.21(b)(2) If necessary, the PBGC will allow majority owners (50% or more) to forego (with spousal consent) enough benefits to make the plan assets sufficient. Revenue Ruling 80-229, Section 4.02(2) states that "assets shall be allocated, to the extent possible, so that the rank and file employees receive from the plan at least the same proportion of the present values of accrued benefits (whether or not nonforfeitable) as employees who are officers, shareholders, or highly compensated". The IRS does not administer §4044 of ERISA, the PBGC does. For the IRS, this is an asset allocation issue that must be non-discriminatory (i.e. not in favor of Highly Compensated Employees - HCE) under IRC §401(a)(4). HCE include all substantial owners per IRC §414(q) because it includes 5% owners. The IRS is also concerned about non-forfeitability under §411(a), anti cutback rules under IRC §411(d)(6), and anti-alienation §401(a)(13) rules-Technical Advice Memorandum 9146005 (July 5, 1991). The checklist in IRS Announcement 94-101 (Field Examination Guides) appears to show that the IRS will allow majority owners to waive their benefits to make a plan sufficient (Section 592, 5 (11)(4)). The IRS may not allow minority owners (less than 50% ownership) this opportunity because of the concern that majority owners could force minority owners to "waive" their benefits. In this case, the owners might just fund the plan and get the money back as a lump sum. The IRS will not allow a "waiver" of benefits to correct an Accumulated Funding Deficiency in the Minimum Funding Standard Account, per Technical Advice Memorandum 9146005. Another technique used to make plans sufficient, is to have majority owners state in writing to the Insurance Company that they will not elect the subsidized lump sum or early retirement options.

(12) Standard Termination Notice to PBGC: After or at the same time the Notice of Plan Benefits is issued (not received), the Plan Administrator must send a notice to the PBGC using Form 500 and Schedule EA-S. The law requires this form be sent as soon as practicable. Regulation §4041.25 states that this Form must be filed no later than 180 days after the proposed DOPT. In order to provide even more time, the proposed DOPT can be changed to a later date but in no case later than 90 days after the NOIT. If more time is needed, you can start the process over, send out the NOIT, NOPB, and Form 500 quickly, and not delay distributions much at all. The PBGC has been known to extend the deadline due to National Disasters such as floods (hurricane Katrina in 2005) and earthquakes (L.A. in 1994).

The PBGC acknowledges receipt of your Form 500 filing and provides the date they received it, so that the plan administrator will know when the 60-day PBGC review period has expired. If you never receive the acknowledgment, you may want to call the PBGC at (202) 326-4000 to ensure they received the Form 500 filing.

Contents: The Form 500 requests information on the plan, reasons for the termination, information on a replacement plan (if any), the dates of proposed DOPT, NOIT, Notice of Plan Benefits (to see if deadlines met), whether there will be an employer reversion, and the date of plan amendments allowing reversion (to ensure it was adopted over 5 years before termination or at plan adoption). If a spin-off or other transfer of assets or liabilities has occurred within the last 3 years, then the Plan Administrator will have to certify that the Joint Implementation Guidelines (Appendix B) have been followed. (See the section in this chapter on Withdrawing Assets from a Plan.)

Schedule EA-S asks for projected assets at proposed date of final distribution and the value (as of final distribution) of all benefit liabilities (accrued as of DOPT). The value of the plan's benefits that are payable as an annuity should be based on an estimate of the bid prices of insurers. The form essentially is asking the actuary to certify that assets are sufficient for all benefit liabilities; thus, if assets are much more than liabilities, the actuary does not need to get an actual bid price from an insurer. The actuary should reflect Employer Commitments and majority owner "waivers" in the above amounts in order to show sufficiency. Form 500 includes the plan administrator's certification that the information supplied to the actuary is correct and that the P/A will keep all records for six years. The Enrolled Actuary should ensure that individual benefit calculations are accurate (not estimates). In one case (Boatwright), a court held the actuary and the plan sponsor liable for undervaluing benefit liabilities (by not including participants, undercutting participants' benefits, and not valuing them appropriately) and for taking too much of a reversion. They were convicted and the actuary lost his EA enrollment status and went to jail.

Be careful to complete all the items on the PBGC forms. The PBGC has the authority to restart its 60-day review period if the forms are not completed properly. This only delays distribution of assets. However, it could force the plan into a new plan year and that could mean larger lump sums; so be sure you have fully completed your Form 500. More likely, the plan administrator can preserve the original 60-day review period by quickly correcting any errors brought up by the PBGC. See a further discussion on this in the section of Notice of Non-Compliance.

(13) A challenge from a collective bargaining unit stops the clock until resolved by the outside parties and can undo the termination process per §4041.7 (even if it occurs after the end of the PBGC review period). For example, a suit by the USW and retirees against United Engineering (formed in a 1986 divestiture of former Wean United Inc. operations in Youngstown and Canton, Ohio) alleged that the Distress Termination violated the bargaining agreement. The parties eventually agreed to a settlement which delayed DOPT another 9 months. Since United Engineering had stopped payment of the retirees $400 supplements at the proposed DOPT, United had to pay 9 months X $400 = $3,600 to the 200 retirees, or about $700,000. The PBGC agreed to trustee the plan only after a Cleveland federal judge approved the settlement. The PBGC did not do anything until the suit is settled, and then took over the plan. An actuary should get assurances in writing from the plan sponsor that termination does not violate a collective bargaining agreement and that there is no challenge.

(14) PBGC Review (§4041.26)/Notice of Non-Compliance (§4041.31): If the PBGC has been given the Form 500 and has not responded with a notice of non-compliance within 60 days (with extensions) of the Form 500 filing, the plan administrator may commence final distribution (as long as assets are still

sufficient for all benefit liabilities). The PBGC acknowledges all filings, usually within 2 weeks. Therefore, if you have not heard from the PBGC within 60 days, do not assume that they have received and reviewed your filing (i.e. do not distribute yet – call them).

Notice of Non-Compliance (NONC): A small number of filings receive a "Notice of Non-Compliance", typically because they fail one of the rules or deadlines in the law. If a Notice of Non-Compliance (NONC) is issued, it will prohibit the proposed termination, making the plan ongoing. It will also provide the employer with the steps that must be taken to request a reconsideration, and information on how to inform the employees. Examples are:

- The NOIT was not filed 60 full days before the proposed DOPT.
- The Form 500 filing did not occur by the deadline in the regulation.
- The NOIT and/or the Notice of Plan Benefits were not issued before the Form 500 filing.
- There is sufficient reason to believe that the plan is not sufficient for all plan benefits. If the sponsor commits to make the plan sufficient, include the value of such commitments in asset amount on Form EA-S. Otherwise, the PBGC will issue a NONC.

A plan has 30 days to request reconsideration in response to a NONC. Otherwise, the devastating effects of a NONC are:

- The plan is ongoing-including accruals (unless plan was frozen),
- vesting, and compliance with new laws must continue,
- lower interest rates may cause bigger lump sums,
- affected parties must be notified per 4041.31(g) that the plan wasn't terminated,
- actuarial valuations and Form 5500 with Schedules B must be filed for the intervening plan years, and may be late and thus subject to filing penalties. Funding deficiencies may have occurred causing excise taxes.
- PBGC forms may have to be amended, if the sponsor had used the Standard Termination exemption to the variable premium requirements.

If the termination was denied on account of (1) not following the termination rules or (2) the plan being insufficient, then:

- In-service distributions may have occurred, causing disqualification because of a pre-ERISA rule {Regulation §1.401-1(b)(1)(i)}, which states that benefits may be distributed only upon retirement, disability, and death. IRC §401(a)(20) and Revenue Ruling 74-254, 1974-1CB.91 also allows distributions upon termination of the plan or termination of employment.
- After the appeal period runs out, the PBGC will send notices of the NONC to the IRS, which could hurt the determination letter process.
- The plan could become disqualified, thereby losing tax advantages and deductibility. Distributions would become taxable and/or subject to penalty.

If the plan sponsor still wants to terminate the plan, then:

(a) the whole process must be repeated
  - NOIT (which could be confusing to participant the second time)
  - Notice of Plan Benefits
  - Form 500

(b) the possibility of poor asset returns could result in loss of Standard Termination status or a smaller reversion to the sponsor (or participants)

(c) It will delay distribution of benefits to participants.

The PBGC would prefer not to "NONC" a plan. ERISA §4041(b)(2)(c)(i) allows the PBGC to avoid a NONC if it is inconsistent with the interests of the participants. Even if a NONC is avoided, the PBGC could still assess penalties. PBGC has stated it may waive the NONC if benefits were frozen, top-heavy rules do not mandate benefits to non-key employees, and participants would not be helped by a NONC.

(15) Favorable Determination Letter: Assuming the 5310 filing was timely, wait for the IRS determination letter before proceeding to the final distribution of assets.

(16) Insurance Company Contracts: Start the process of finding an insurer as soon as possible. The 60-day distribution deadline after receiving the IRS determination letter does not provide enough time to do this. Irrevocable commitments (single premium, nonsurrenderable annuities) must be purchased for everyone who does not elect a lump sum or receive a mandatory lump sum and they must preserve all benefits, forms, options (including future lump sum elections), rights, and consent requirements in the plan. See Chapter VI for what is in benefit liabilities. The commitment is not irrevocable if the insurer sends one "bulk payment" to a third party to distribute among participants, unless the insurer promises to distribute if the third party fails. Some insurers may require a non-refundable deposit for the bids to remain outstanding for the long period needed to implement a termination. If the actuary is certain that assets will be sufficient, then a formal commitment from the insurer (a qualifying bid) is not needed up front for completing PBGC Forms.

One interesting note: an Insurance Company as plan sponsor may need to be careful if it sells its pensions to itself and inflate the price in order to reduce the reversion and hence the excise tax and income tax.

Participating contracts may be used if all benefit liabilities are covered by an irrevocable commitment backed by the insurer's full general funds and if the employer and insurer so notify the IRS (GCM 39765). A DOL letter dated 11/18/86 states that the decision to purchase a Par Contract is subject to ERISA fiduciary standards. Regulation section 4041.28(c)(4) states: "In the case of a plan in which any residual assets will be distributed to participants, a participating annuity contract may be purchased to satisfy the requirement that annuities be provided by the purchase of irrevocable commitments only if the portion of the price of the contract that is attributable to the participation feature—
(i) Is not taken into account in determining the amount of residual assets; and
(ii) Is not paid from residual assets allocable to participants."
Thus, in a contributory plan, where some residual assets are due to employees, a non-par bid will be needed to determine the residual or surplus.

45-Day Notice of Insurer: PBGC regulation §4041.23(b)(5) requires plan administrators to inform participants in the NOIT of the insurers that will be used. If the insurer has not been decided on at that point, a short list of insurers from which they will choose must be provided. This gives the participants a chance to object to the insurance company. (See the following section on Fiduciary concerns.) This may encourage more employees to choose lump sums, since they must also be told that the PBGC guarantee ceases upon distribution of the annuity.

At least 45 days before the actual distribution, the plan administrator must notify participants and the PBGC of the name of the insurer and information on state guarantees, per PBGC regulation 4041.27(d). Note: PBGC says the notice must be provided to participants even if they all elect lump sums, because they have the right to switch to an annuity. The only participants that do not have to receive the 45-day notice are those getting mandatory lump sums.
The following are important considerations for annuitizing.

- Prepare in advance for the purchase of annuities.
- Immunize your assets through duration matching. You will probably prefer high quality fixed income assets with good liquidity. Involve the asset manager up front. You will need to pay the insurer quickly!
- To get the best price:

1. Don't lock in annuity purchase way in advance of the actual distribution of money to the insurer unless you have to in order to preserve sufficiency. Maybe you could do this through immunization techniques.
2. The PBGC does not require the plan to lock in a purchase price before filing the forms. This will minimize hedge costs/interest rate volatility. Wait until the PBGC review period is over and the determination letter arrives before distributing.
3. It may help reduce the bid price if you give the insurer your mortality, retirement, disability, and election experience.
4. Tell insurer that you will definitely buy (they don't need practice quoting).Predictable cash flows are preferred (e.g., monthly retiree benefits and survivor benefits).
5. Unpredictable cash flows caused by lump sums, and future death and disability benefits add volatility and increase the price; so amend death and disability benefits out of the plan to the extent possible. Don't add a subsidized lump sum provision; lump sums determined at GATT rates or Treasury rates are preferable because they swing with the value of duration-matched assets.
6. Contributory plans add complications; take longer to process; and add to costs. Can you pay these out before annuitization? Plans with offsets from another plan (or insurance company annuity) also add complications.
7. Segment your benefit liabilities into short and long durations. Some Insurance Companies will prefer one or the other to keep their assets and liabilities cash matched (or duration matched). They may also have different preferences due to different Income Tax positions.
8. Purchasing at the end of year may be a bad time to annuitize if insurers are having problems with surplus strain caused by reserving above pricing.

- In order for the final bid to be processed quickly, prepare all data in advance in electronic form and work with insurer in advance so they are ready.
- You will need old plan documents (now) and birth certificates (later).
- Insurers typically take two to four weeks to provide a quote for a moderate-size plan.
- Picking the Insurance Company (Note the typical plan actuary is not qualified to consult regarding this decision. This is a fiduciary decision, and the actuary should encourage the client to seek appropriate expert advice for this decision).
  1. Price is important, but so is security. Review past and present credit ratings at Bests, S&P, Duff & Phelps, Moodys, and Weiss. Also review their Annual Statements for the quality of their assets. Do they have much junk bonds or non-performing real estate? Are they backed by State Guarantee Funds? Up to how much? Reinsurance?
  2. Experience of carrier: Has insurer been in the business for a long time or are they in and out based on profitability? Can they administer your pension plan? Separate Pension Units may be better.
  3. Review bid to ensure that all options and elections in plan are covered (e.g., they must use plan factors, not actuarial equivalents).
  4. Review how bid price is adjusted for participant data changes.
  5. Does insurer pay by "bulk deposit" and have back up distribution capabilities/promise?
  6. Does insurer have direct deposit, 800 number for participant questions, willingness to take/pay small amounts, willingness to find annuitants at normal retirement age?
  7. Will the insurer allow the bid to stay open long enough for you to distribute?
  8. Will the insurer return your initial deposits if the termination fails the PBGC Review?
  9. The plan administrator should ensure that the insurance company (and the trustee paying lump sums) will send out Form 1099-R's before January 31 of the following calendar year.

(17) Fiduciary Concerns: Some decisions may be subject to fiduciary standards. According to the DOL letter of March 13, 1986 in Appendix B, **fiduciary decisions include**:

(1) the choice of an interest rate in determining lump sum amounts (Note: §401(a)(25) eliminates discretion here now),

(2) the choice of an insurance company (it's an investment decision and insurance companies are subject to default), and

(3) the interpretation of plan documents to determine benefits and whether a reversion is allowed and the amount of the reversion.

However, three judges on the 3rd Circuit unanimously affirmed a lower court's dismissal of plaintiffs suit regarding an employer's selection of a mortality table and interest rate used to convert the employee's traditional DB plan benefit to an account balance in a new Cash Balance plan (Corcoran v. Bell Atlantic Corp., 3rd Cir., No., 97-1926, 7/30/98). It was also held to meet the §411(d)(6) anti-cutback rule.

Not providing **good, honest advice** to participants is also a **fiduciary breach**. In Vartanian v. Monsanto Co., CA1, No. 93-1611, 2/2/94, the First Circuit reinstated an employee's claim that Monsanto breached its fiduciary duties in failing to provide complete and truthful information to Vartanian's questions (before he elected retirement) about rumors that early retirement benefit improvements were imminent. However, the Sixth Circuit held the opposite in Swinney v. GM (CA6, No. 93-3872, 1/30/95) probably because the fiduciary honestly told the participant that they didn't know if the plan would be improved. See similar decisions in Taylor v. People's Natural Gas (CA3, 1995 US App Lexis 4622, 3/9/95), Wilson v. Southwestern Bell Tel. Co., 1995 U.S. LEXIS 11784 (8th Cir. 1995), and Muse v. IBM Corp., CA 6, No. 95-6261, 12/26/96.

Several courts have ruled that **the decision to terminate a plan** is not subject to ERISA fiduciary standards. See, e.g., Champ v. American Public Health Assoc., 8 EBC 2217 (D.D.C. 1987).

In Horan v. Kaiser Steel Retirement Plan, 14 EBC 1968 (9th Circuit 1991) the Pension Committee **stopped purchasing annuities** because plan assets would eventually be eliminated due to those purchases. The Pension Committee's decision to stop purchases shortly before the plan was terminated with insufficient assets was held to not be a fiduciary violation, because the court held that it was not arbitrary, it did not hurt the plan as a whole, and the annuity purchases were not promised in any plan documents.

In addition to the Horan v. Kaiser case, plan participants sued the Kaiser plan actuary for knowing involvement in the underfunding of their plan (e.g., did they adequately reflect higher early retirement rates?) in Mertens v. Hewitt Associates, 14 EBC 1973 (9th Circuit Court 1991). Hewitt was held not liable because the **actuary is not a fiduciary** (even though the actuary may have been a "knowingly participating individual"). The Supreme Count affirmed that Hewitt was not a fiduciary in Mertens v. Hewitt Associates, 16 EBC 2169 (U.S. Supreme Court 1993) but did not address the specifics of the plaintiffs claim against Hewitt. The Department of Labor supported the plaintiff (Merten's) and hoped Congress would overturn the Supreme Court decision. It didn't.

In Howard v. TWA (N.D. Ill. 1991) it was found that an actuary's termination work papers were subject to **discovery**. This is especially true if they are the actuaries for the plan and for the sponsor. They could be exempt from discovery if they were prepared for the sponsor's lawyers in response to (or possibly in anticipation of) litigation. The only way to be sure you are not the actuary for the plan and the sponsor is to convince the employer to get a separate actuarial firm for the plan.

Paying expenses from Plan: Per ERISA 403(c)(1), pension plan assets can only be used for providing benefits to participants "and defraying reasonable expenses of administering the plan." A DOL Information Letter (in Appendix B) said that paying expenses for terminating a pension plan is a question for the fiduciary. Fees for ongoing actuarial valuations, etc. are permitted if they are reasonable and if the plan and trust so provide. If an actuary or attorney is paid from the plan, the attorney-client privilege may be lost by the sponsor. At this point, the plan and its participants may become the actuary's/attorney's client. This could require them to divulge sensitive information to participants. When not paid from plan assets, the Second Circuit [Board of Trustees of the CWA/ITU Negotiated Pension Plan v. Weinstein, 1997 US App LEXIS 3271 (2/24/97)] stated that participants are not necessarily entitled to the plan's actuarial reports (in direct conflict with the Sixth Circuit).

DOL suggests that some functions performed in conjunction with the establishment, termination, and design of plans are **Settlor Functions** and probably should be born by the Sponsor as they serve the sponsor's interest. For example, terminating a plan reduces the sponsor's cost and generally does not help participants. Thus, the expenses for deciding *whether* to terminate should not come from the plan. However, the required Notice of Plan Benefits helps participants, so the plan probably can pay for this and other similar functions. DOL Opinion Letter 97-03A states that amending the plan and filing for the final determination letter can help participants and the sponsor, so an independent fiduciary could apportion those expenses to the plan and sponsor. Also, be careful if assets are close to liabilities and could reduce participants' benefits if paid. On the other hand, if a company is bankrupt, Settlor expenses might help participants get something they otherwise would not.

Annuity Purchases: The PBGC requires information on potential insurers be sent to affected parties. The information must be sent to affected parties other that the PBGC at least 45 days before the annuity purchase becomes final. This information allows any affected party concerned about the safety of the insurer to raise objections before the final purchase of the annuities. The PBGC does not need to be informed of the name of the insurer until the post distribution notice late in the process.

The fiduciary should be **prudent** and pick a well-rated insurance company and have evidence that the insurer is solid. Fiduciaries should also see that the Insurance Co. is well reinsured and/or covered by State Guarantee Funds. It will be helpful if you document the reasons why you chose your insurance company. The ACLI suggests you select an insurer that does not invest heavily in junk bonds or non-income-producing mortgages or have assets concentrated too much in a single area and suggests that one review:

(1) the NAIC state accreditation guidelines,
(2) the insurer ratings, and
(3) the number of years the insurer has been issuing annuities.

The PBGC and DOL agree that the **failure of an insurer** is a Title I fiduciary question, not a Title IV question. The PBGC cannot charge a premium for annuitized participants (as they are no longer participants in the plan), cannot regulate the insurance industry (nor do insurers want federal regulation from the PBGC), and has determined that it is not authorized to guarantee the annuities because the only insurable event that triggers benefits is termination. (If Congress had wanted PBGC to stand behind insurance company annuities, it is figured that they would have been clearer about it, e.g., they would have set the premium amounts.) In addition, the PBGC felt that guaranteeing annuities could (1) cause imprudent and abusive practices in the Insurance industry, (2) result in state guarantee funds removing their guarantees of pension annuities, and (3) make the guaranteed benefit very complex to calculate without necessary employer documentation. Insurers may not want PBGC to insure the benefits either, since that might subject them to PBGC premiums and regulations on their assets, etc.

DOL Interpretive Bulletin (IB) No. 95-1 relating to the fiduciary standard under ERISA when selecting an annuity provider[4] states that "fiduciaries... [must] take steps calculated to obtain the safest annuity available, unless under the circumstances it would be in the interest of participants and beneficiaries to do otherwise." Per DOL, more than one annuity provider may be able to offer the safest annuity. If participants get some or all of the reversion, then a cheaper bid may be the best choice. Thus, a plan could be amended to give participants a portion of the surplus and this would relax the standard. DOL warned, that this could never be the justification for buying an "unsafe" annuity however. The IB warns that sole reliance on ratings is not sufficient and lists the following 6 factors as illustrative of things to consider:

(1) the quality and diversification of the insurer's portfolio,
(2) the size of the insurer relative to the proposed contract,
(3) the level of the insurer's capital and surplus,
(4) the lines of business of the annuity provider and other indications of an insurer's exposure to liability
(5) the structure of the annuity contract and guarantees (such as use of separate accounts)
(6) the availability of additional protection through the state guarantee associations and the extent of their guarantees.

The IB also states that the fiduciary will need to obtain and follow independent expert advice, especially where a conflict of interest may exist (which is often since the employer gets more reversion or has to pay less to top up the plan when the bid is cheaper). This DOL IB also applies when purchasing annuities for individuals upon separation of employment, but does not apply to annuities held by the trust as an investment. Companies using a DA or IPG-type contract at an insurer which is not "safest", may have to purchase annuities upon retirement from another insurer or they will have to remain as the contract holder for the retirees' annuities. The Information Bulletin is effective back to January 1, 1975, the date ERISA fiduciary standards under Title I were effective.

After Executive Life failed to pay the full amount of their contracted benefits, the IRS issued Rev. Proc. 92-16 and Rev. Proc. 95-52[5] to let employers (that used Executive Life) make their DC plans whole. Some of these ideas may be helpful to DB plans. If the sponsored feared that participants might sue for fiduciary breach, they were able to make up the loss by applying for a prohibited transaction with DOL (or qualify for a class exemption). If the sponsor had applied to the IRS for a closing agreement, then the following IRC problems were waived.

(1) Not paying the full benefit could have jeopardized compliance with minimum distribution requirements of §401(a)(9).
(2) Making participants' benefits whole may increase HCE benefits too much and thus not meet the non-discrimination rules of §401(a)(4).
(3) A company paying full benefits now and getting reimbursed later when Executive Life is purchased could violate the non-diversion rules of §401(a)(2).
(4) Lump sum treatment of distribution could be lost if the lump sum is paid in parts.
(5) Contributions in DC plans could exceed the §415(c) limits.
(6) Exclusive benefit rule.
(7) Excise taxes on non-deductible amounts.

It may also provide relief from:

(1) anti-cutback rules of 411(d)(6) for when full benefits are not distributed, and
(2) latest benefit commencement rules of 401(a)(14), when benefits are delayed.

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4 The DOL IB can be found at http://www.dol.gov/dol/allcfr/Title_29/Part_2509/29CFR2509.95-1.htm
5 This Revenue Procedure is in the 1995-2 Cumulative Bulletin at http://www.irs.gov/pub/irs-irbs/cb95-02.pdf

The DOL will also allow a company to pay full price for an Executive Life GIC which has lost its value. Normally this would be a prohibited transaction (not paying market price), but DOL will give an exemption here. One problem may remain. The conditional contribution may still not be fully deductible under §404. The closing agreement will specify the amount deductible currently and how much will be deductible in the future.

(18) Distribute Payment Election Forms and Required Notices: These include the notices of available options, QJSA notices, tax notices, insurance company notices, etc., unless distributed earlier, but within the time constraints required for the various notices. If payment election forms are distributed now, the schedule needs to allow time for the participants to complete them and return them. The insurance company's final bid should reflect the actual benefit option elected, if irrevocable. Benefits will be paid under the default option if no election is returned. This most often means an annuity will be purchased for someone who could have elected a lump sum, but who did not respond to the election form mailing.

(19) Employer Contribution: Once the exact cash requirements for lump sums and the annuity purchase is known, the employer must contribute any amount necessary to provide sufficient assets to terminate the plan.

(20) Final Distribution: After the 60-day PBGC review period, the plan administrator may commence final distribution as long as assets are still sufficient for all benefit liabilities on the distribution date.

If assets are insufficient, the plan is ongoing and the plan administrator (P/A) must notify the PBGC and participants promptly - 4041.28(b) . The PBGC at its discretion may allow conversion to a Distress Termination, if all Distress conditions are met, but the PBGC expects approval to be extremely rare.

A **distribution** has not been defined to occur until the obligation to provide benefits passes to the insurer (or the participants have received their lump sums). According to Regulation Section 4041.28, distribution must occur within 180 days after the end of the 60 day PBGC review period (with extensions). If distribution is not timely, the PBGC can NONC your termination (i.e., abort it). Extensions have been granted for floods and earthquakes, etc. The PBGC may approve other extension requests. Regulation 4041.28(a)(1)(ii) also allows an automatic extension to 120 days after receipt of a favorable IRS determination letter, if the determination request was filed on or before the date the termination notice to the PBGC was filed. The PBGC may approve other extension requests. Note: Neither the PBGC nor the IRS want this to turn into a frozen plan or wasting trust. See IRS Revenue Ruling 89-87, which says assets must be distributed "as soon as administratively feasible" which the IRS has interpreted as within 1 year of DOPT or until 6 months after the determination letter is issued if the request was timely-filed. The PBGC says it's "as soon as practicable" language in 4041 does not allow for "my actuary was too busy". Only if it was outside the plan sponsor's control would the PBGC allow extensions. Examples of this are the Union stalled the process, the factory flooded, or the accountant stole the money and records. Not being able to liquidate assets is not good enough, as the PBGC would say "you do not have a terminated plan." The IRS, in Revenue Procedure 92-10, has provided plan sponsors liberalized lump sum tax treatment and some accommodation on minimum distribution rules when assets are tied up at an insolvent insurance company.

(21) Missing Participants: The Social Security Administration may help in locating missing participants. Just provide the SSN, per Rev. Proc. 94-22. If under 50 people, the IRS District Office will help for free but may only be of help for filers in their region. If over 49 people, the IRS National Office can help for a fee. TRW, Equifax, Donovan, Clark, and Company (Illinois), Pension Benefit Information (California), Credit Bureaus, and State Bureaus of Vital Statistics can also be helpful in finding missing participants. If

some participants still can not be located, the PBGC requires purchasing irrevocable commitments (annuities) to provide benefits for each participant. Another solution on "unlocatables" is to move their liability to a replacement plan. RPA 94 added §4050 to ERISA to help plan administrators here. Per final PBGC regulation 4050, the PBGC will take over the responsibility for handling the participants that are still missing after a plan has performed a diligent search. A search is diligent if:

(a) it is begun in time to make distributions with the other participants,
(b) beneficiaries and alternate payees of the missing participant are contacted for help, and
(c) a commercial locator is engaged (i.e., the IRS is not good enough).

For each missing participant for whom an irrevocable commitment is not purchased the Plan must file Schedule MP with the Post-Distribution Certification and pay to PBGC:

(a) the plan's lump sum amount if # $5,000. PBGC then pays participant such amount with interest, even if over $5,000 (breaching 417)
(b) the PBGC lump sum using the unisex UP84 and the old PBGC interest rates at the most valuable retirement age (ÎNRA) if the plan has no mandatory lump sum and if # $5,000. PBGC then pays participant such amount with interest.
(c) the PBGC present value of the accrued benefit at the most valuable age (or plans lump sum value if greater) if the lump sum is > $5,000. The PBGC will pay the actuarial equivalent (using PBGC assumptions at the time the funds are received) in its standard forms: LO, QJ&S, or Lump Sum (if in plan). This breaks rules that plan must provide all options, elections, waivers, rights. IRC §401(a)(34) keeps this from becoming a qualification problem. Plans should reference §4050 in their plan document per ERISA §206(f).

Schedule MP informs PBGC of (a) the Insurance Company used (in case missing participants show up), (b) information to help identify and locate missing participants, and (c) how to compute their benefits. The EA must also certify that benefit amounts are correct. Note that the check to the PBGC goes to a different address than the Form 501 or Schedule MP. The Schedule MP also requests that you attach the QPSA waiver, the optional benefit form (and QJSA waiver), beneficiary designation, and any QDRO's.

(22) Post-Distribution Certification: The employer must file a certification using PBGC Form 501, within 30 days after distribution of all benefit liabilities that assets were sufficient and distributed in accordance with law. Do not wait for distribution of the excess assets. The PBGC will send you a reminder if they never get your Post-Distribution Certification.

Penalties: Late Form 501's incur a daily penalty. PBGC has decided to waive penalties until 90 days after the distribution deadline, per PBGC Statement of policy dated 3/14/97 in 62FR12521. A revised PBGC Statement of Policy issued 7/18/95 in 60FR137 suggests that the late fee be the smaller of $50 per day or $100 per participant. The first 90 days of delinquency were reduced to half of the $50 or $25. In addition, PBGC proportionately reduces the daily penalty for plans with less than 100 participants.

Except for data on missing participants, individual employee data is not to be included with Form 501, but the certification must state the location of the data and the name of the insurer, if any, who is providing the benefits. The employee data, plan documents and worksheets must be maintained and preserved by the plan administrator for six years after Form 501 is filed. The plan administrator must make these records available to the PBGC within thirty days if requested. A copy of the Insurance contract or certificate must be sent to participants on or before the due date for Form 501. If unavailable at that time, the plan administrator must notify the participants of the contract and other items per 4011.27(g)(2), but participants must still get a copy of the contract or cert when available.

(23) Pay Asset Reversion (if any) to Employer: Once provision is made for all annuities, lump sums, amounts for missing participants (see below), and reasonable expenses, the remaining amount may be set aside for the reversion to the employer and any excise taxes thereon. The reversion should be taken soon thereafter if allowed by the Plan and the SPD and law. (Please see the section on Residual Assets in Chapter VII.) The reversion (including the value of the participating portion of a par contract) is subject to an excise tax (payable on the last day of the next month per IRC §4980), unless the sponsor has always been tax exempt[6] or in bankruptcy on DOPT. The reversion is also subject to the Federal Income Tax. Note: The excise tax is owed on reversion amounts returned to federal agencies by government contractors. See Private Letter Ruling 9136017. Hopefully the government agency would only request the net reversion, since Federal Acquisition Regulations (FAR) state that punitive-type taxes (e.g., an excise tax on reversions?) are not reimbursable costs under government contracts effective March 26, 1996 [61 FR 2641 (January 26, 1996)].

Due to OBRA90, the excise tax on any amount of asset reversion to employers from a terminated qualified defined benefit plan was increased from 15% to 50%. Under IRC §4980(d), the excise tax is only 20% if an employer (1) allocates at least 20% of the maximum reversion to provide for pro-rata benefit increases in accrued benefits for all "qualified participants"[7] or (2) establishes a "qualified replacement plan". Note that the pro-rata allocation in item (1) cannot cause the plan to be discriminatory in favor of HCEs and not more than 40% of the reallocated benefits can go to qualified participants who are not active. The §415 limit cannot be exceeded although the 10-year limitation in §415(b)(5)(D) is waived, per 4980(d)(4)(C). Termination could also wait until the 415(b)(1)(A) limit increases $5,000 (to use up the surplus).

Qualified Replacement Plan (a new or existing DB or DC plan): (i) at least 95% of the active participants in the terminating plan who remain as employees must be active employees in the replacement plan, and (ii) the amount transferred to the replacement plan plus the amount allocated to aggregate benefit increases in the terminated plan is 25% of the maximum reversion. Note: Per PLR 9823051, if more than 25% is transferred, the portion in excess of 25% (it appears that the IRS will tolerate de minimis differences) shall be taxed as a reversion. This portion in excess of 25% is: subject to a 20% excise tax (since the employer met the requirements for a replacement plan), treated as income for purposes of Federal Income Tax (FIT) and if allowable, deducted as a plan contribution. NOTE: 1) the benefit increases in the terminated plan must be in the last 60 days and don't have to be pro-rata and don't have to be to everyone, 2) the opportunity exists for people not participating under the terminating plan to benefit from the funding of the replacement plan by this transfer. Additional requirements are imposed if the replacement plan is a defined contribution plan. For example, if after 7 years, the surplus moved to the DC suspense account has still not been fully allocated, the remaining unallocated amount will be subject to excise tax. This is still a good deal, since 75% of the original reversion had an excise tax of only 20%.

The excise tax can be eliminated if the entire surplus is allocated to participants in the plan or to a §401(h) retiree health account according to §420. (Note that amounts not used in the current year in the retiree health account would be subject to an excise tax.) Does some of the surplus belong to those

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[6] If one of the plan sponsors in the past was not tax exempt, then the full tax may be payable, not just a pro-rata portion. I.E., the for profit could forever fully taint the tax exempt.

[7] "Qualified Participants" includes: (i) active participants; (ii) pay-status participants; (iii) separated employees with a non-forfeitable right to a benefit under the terminated plan at DOPT who terminated within the period three years before DOPT up to the date of distribution. Thus terminated vesteds who received lump sums in the last three years are not included.

participants who made contributions to the plan? No. See Chapter VII, Section 9 regarding Residual Assets on contributory plans.

Other ways to reduce the reversion are:

- continue plan and take funding holidays before termination;
- paying expenses out of the trust (including salaries of the company's benefits personnel and their rent) to the extent permitted;
- merging with an underfunded plan before termination
- spinning off more assets than liabilities to an underfunded plan for a higher sale price (although you should investigate that this not be deemed a reversion.
- pay subsidized optional conversion factors on the company's DC account balances from the DB plan. This can even be done for people at the DB and DC maximums, because the subsidized benefits on DC account balances are still considered a DC benefit for 415 purposes per 1.415-3(b)(1)(iv) and don=t change the 415 maximum calculation. Also see the example 4 at section 1.415-7(e).
- transfer just liabilities (not assets) from another plan into the overfunded plan (a naked liability transfer).

This last idea is often done between a company's hourly and salaried plans when transfers occur, but can probably be used in many other situations, as long as the plan receiving the liabilities is in a surplus situation after the transaction. A Technical Advice Memorandum [TAM 9516005] from IRS also allowed an employer paying supplemental benefits from its general assets to use its pension plan to assume the liability. Not all employees supplements were moved to the plan because some large ones for HCE's might have hurt their chances of passing the general nondiscrimination tests. IRS said it was acceptable because

(1) they were pension type benefits,
(2) they satisfy the QJSA rule,
(3) are payable only to "employees or their beneficiaries" with respect to the Plan [per the exclusive benefit rule in regulation 1.401-2(a)(3)], and
(4) they don't cause the transfer to be a prohibited transaction under 4975(c)(1)(D) because they are for the participants (even though it does give an "incidental benefit" to the employer).

Note: It is unclear whether the employer got the approval of DOL, which is generally where prohibited transaction exemptions emanate from for ERISA §406(a)(1)(D), which is identical to IRC §4975(c)(1)(D). The transfer could also cause self-dealing restrictions under 406(b)(1) or (2). Also see the Fiduciary Concerns section of this chapter regarding using pension surplus to finance hostile takeovers (Kayes v. Pacific Lumber Company 9th Cir. 4/10/95) and the transfer section in Chapter X.

It is not clear if surplus from the DB plan can be used for 414(k) DC-type accounts in DB plans. A private letter ruling 9723033 said that moving DB surplus to a 401(k) account would constitute a reversion and disqualify the DB plan (for using the surplus, not for exclusive benefit of participants but inuring to the benefit of the employer).

Net Reversion to Employer (Numerical Illustration)	Straight Reversion	Qualified Replacement Plan	Prorata Increase To Qualified Participants	Residual To Participants
1. Market value of assets	$11,000	$11,000	$11,000	$11,000
2. PBGC termination liability	$10,000	$10,000	$10,000	$10,000
3. Maximum reversion (1) - (2)	$ 1,000	$ 1,000	$ 1,000	$ 1,00 0
4. Cost of providing additional benefits	0	250	200*	$ 1,000
5. Reversion subject to excise tax (3) - (4)	$ 1,000	$ 750	$ 800	$0
6. Excise tax rate	50%	20%	20%	N/A
7. Assumed corporate federal tax rate	35%	35%	35%	N/A
8. Total tax rate (6) + (7)	85%	55%	55%	N/A
9. Amount payable to IRS (5) x (8)	$ 850	$ 412.50	$ 440	$ 0
10. Net reversion to employer (5) - (9)	$ 150	$ 337.50	$ 360	$ 0

*Employer assumed to elect 20% increase, although any percentage between 20% & 100% is permitted.

(24) Pay Excise Tax: Use Form 5330 to pay any excise taxes due to reversions or non-deductible contributions.

(25) Form 5500, Schedule B, and PBGC Form 1 (or subsequent filing form or method) still need to be completed for the final plan year. The minimum funding standard account must be maintained through the end of the plan year in which termination occurs. Charges and credits are pro rated for the short year (Revenue Ruling 79-237). Minimum contributions must be paid even though assets exceed liabilities (Lee Engineering Supply Co. v. Commissioner, U.S. Tax Court, No. 19267-90, 101 T.C. No. 12, 8/30/93).

Effective 1/1/95, Revenue Procedure 95-51, section 4.03 allows plans with assets (not including receivables) exceeding benefit liabilities to change automatically to the traditional unit credit method in the plan year of termination, use market value assets, and change valuation date to the first day of the PY or the termination date. To use this Revenue Procedure, the plan must:

(1) have not filed Schedule B yet for the PY (and it's not late)
(2) have plan sponsor or plan administrator approve in writing in Form 5500 filing
(3) not have a waiver or be requesting one, and
(4) not be subject to an EP/EO examination

Non-payment of a deficiency results in a 10% excise tax and after notification the 100% excise tax is due if not remedied. Form 5500 and PBGC premium payment forms (with premiums) are due up to and including the plan year in which benefit liabilities are satisfied. The final Form 5500 is due 7 months (extendable up to 9-1/2 months) after assets are distributed. The plan administrator should pay the PBGC an annual premium. PBGC will calculate a pro-rata refund for the portion of the plan year after the date benefit liabilities are satisfied. This includes distributing the surplus allocated to the participants also. When completing the 5500, it will help you down the road if you use Schedule SSA to inform the Social Security Administration that some of the terminated vested employees that they know about from prior Schedule SSA filings have received lump sums. Otherwise, the Social Security Administration will advise the former terminated vested employees to get their pension from the former employer when they reach age 65.

(26) PBGC Audit: Under Section 4003(a) the PBGC must annually audit a significant number of standard terminations. In practice, the PBGC will audit all plans with more than 500 participants, and a significant number of other plans. They may also audit a plan where participants have filed complaints. A sample audit request is in Appendix B. The primary purposes of the audit are to:

- ensure that participants and beneficiaries entitled to a benefit received all their benefit liabilities and that amounts certified to by the Enrolled Actuary are correct.
- ensure that anti-cutback rules of 411(d)(6) were not violated
- respond to participant complaints
- ensure that all PBGC premiums were paid
- ensure that all notices were made timely. (If not, civil actions may be considered and a $1,100 per day fine could be assessed.)
- ensure that annuity contracts provide all elections, notices, benefits, and options to participants.
- ensure the PBGC received the correct amount for all missing participants.

Typical violations that have been caught by PBGC auditors are:

(1) married participants did not get their proper J&S election forms and spousal consent forms.

(2) plans used the statutory interest rates to determine lump sums but forgot that the plan used a lower interest rate and thus had a larger lump sum (and vice-versa).

(3) ages and interest rates for lump-sums were determined as of DOPT, but should have been determined at the annuity starting date (at or near the date of distribution), not at DOPT. The GATT interest rate with a look back to the appropriate month before the year of the annuity starting date can be used if the plan provides such. This is valuable only when interest rates are going down.

(4) some participants did not get their full benefit liabilities.

(5) insurance contract did not provide for all benefit options and elections.

As one can see, the Standard Termination of a PBGC-covered plan can be a long and difficult process. The plan sponsor should be advised about this before starting down that path.

b. DISTRESS TERMINATIONS - ERISA §4041(c) and PBGC Regulation 4041 Subpart C

If a plan sponsor can not make their plan sufficient for all benefit liabilities, then they should see if they can meet the distress termination criteria. Otherwise, they cannot terminate their pension plan although they can freeze accruals (top heavy accruals may still have to be given).

A sponsor can not dispose of a plan by selling it to a weak buyer per Section 4069. For example, Navistar sold its Wisconsin Steel Plant (and plan) to a weak buyer (Envíorndyne). The judge made Navistar pay for its unfunded liabilities as of the sale date.

Problems: You might want to avoid the long and difficult Distress Termination process if you can, because:

(a) It takes a long time.

(b) It slows down the reorganization process (e.g., LTV).

(c) The controlled group generally must go into bankruptcy, which is very expensive.

(d) The filing submission to the PBGC is extensive.

(e) The PBGC guarantee and §4044 allocation process (see Chapters IV through VII) is very complex.

(f) Participants will likely only get guaranteed benefits, though in some circumstances additional benefits can be paid. Participants who have not reached the eligibility date for their subsidized early retirement benefit will be particularly upset. So will:

- partially vested participants
- non-vested participants
- participants over the PBGC maximum
- participant cut by the phase-in of recent amendments (especially Substantial Owners)
- participants with lump sums over $5,000 who now won't get them
- participants with subsidized lump sums
- participants who are not quite eligible for a subsidized early retirement benefit

(g) PBGC claims, participant suits, and union problems will cause untold problems.

(h) Distress Terminations are very closely scrutinized by the PBGC and not many qualify.

(i) The PBGC could restore the plans after all your arduous work (e.g. The Supreme Court restored 3 of LTV's 4 plans back to LTV).

(j) It affects the whole controlled group (CG)

(k) If a company uses the bankruptcy process to qualify for a Distress Termination, it will not be able to improve benefits until the reorganization effective date. ERISA §204(i)

(l) The employer and each member of the CG are jointly and severally liable and will be sued by the PBGC for the full UBL.

Alternatives: A plan sponsor might consider the avoiding a distress termination, by trying for a Standard Termination if the sponsor has the funds to make the plan sufficient. See Section (10) "Commitment to Make Plan Sufficient" in the Standard Termination Section. Ways to reduce the plan's liabilities are

- If interest rates are going down, add a lump sum provision and use interest rates up to 5 months prior to the plan year to determine lump sums. This could produce values below the cost of an annuity, especially the safest annuity, particularly if early retirement subsidies are in the plan but not in the lump sum.
- A majority owner can "waive" their benefits to extent necessary for the plan to be funded through at least guaranteed benefits. The IRS would rather you say you are allocating assets first to non-majority owners.

- Majority owners could promise insurer to not elect subsidized lump sums, subsidized J&S benefits, or subsidized early retirement benefits.
- A large block of annuities could lock in a better rate and be cheaper than subsidized lump sums. (This may not be possible if lumps sums are not available immediately per the plan.) Annuities may also be cheaper than lump sums (which are based on a unisex table) if the plan participants are mostly male or coalminers.
- Use §412(c)(8) substantial business hardship rules to reduce accrued benefits retroactively to the beginning of the plan year (this needs IRS approval which is difficult to get)
- Merge with a over-funded plan.
- Employer can freeze accruals, amend out unprotected benefits, charge for QPSA, and fund the plan (if the resources are available). Note: the plan must continue to meet new laws (e.g., 401(a), coverage requirements, etc.) and may have to provide top-heavy accruals per §416.

Another way to avoid a distress termination, is to reduce contributions, at least until the employer is healthier. For example:

- request a waiver
- use the interest rate at the top of corridor,
- request the funding method with the lowest contribution (e.g., Unit Credit, with projection if required).
- switch to an Asset Valuation Method which reduces the contribution.

Distress Criteria: Per §4041(c)(2)(B), the necessary distress criteria are met if each person who is a contributing sponsor or a member of their controlled group meets any of the following:

(a) Liquidation in bankruptcy (or a bank insolvency receivership action): and not dismissed (negated) by the Court (this is different than the court closing a liquidation). Regulation section 4041.41(e) also stresses that the principal purpose of the liquidation cannot be to evade plan liabilities or otherwise abuse the termination insurance program;

(b) Reorganization in Bankruptcy: the bankruptcy court must determine that liquidation would necessarily follow if the pension plan were not terminated (the PBGC must be given advance notice that the court has been asked to make this determination); or

(c) Termination is required because

(1) unless a distress termination occurs, such person will be unable to pay debts and continue in business, or

(2) the costs of providing pension coverage have become unreasonably burdensome, solely as a result of a decline in work force covered.

All members of the controlled group do not have to meet the same criteria. A review of distress terminations shows that most successful terminations use criteria (a), some use (b), and only a few use criteria (c).

Implementing a Distress Termination: The steps in a Distress Termination are similar to a Standard Termination and are as follows:

(1) The Notice of Intent to Terminate (NOIT) must also be sent to one more affected party - the PBGC - using PBGC Form 600. It also must be provided at least 60 days (but not more than 90 days) prior to the proposed termination date (just like Standard Terminations), unless the PBGC approves a longer period. The contents of the NOIT are similar also, except they must also state the effect of PBGC's guarantees per 4041.43(b)(8) - (9).

(2) The PBGC can set a retroactive DOPT. See Pension Committee for Farmstead Foods Pension Plan v. PBGC, 991 F.2nd 1415 (8th Cir, 1993).

(3) Distress Termination Notice - PBGC Form 601 and Schedule EA-D must be sent as soon as practicable to the PBGC. PBGC regulation 4041.45 allows up to 120 days after the proposed DOPT. These forms help the PBGC determine:

(a) if the necessary distress criteria are satisfied by each member of the CG;
(b) if the plan lacks assets to cover guaranteed benefits and/or "all benefit liabilities" certified by the Enrolled Actuary on Schedule EA-D;
(c) that the plan sponsor has certified to the accuracy and completeness of data used;
(d) who the controlled group of contributing sponsors are, and also which members of the controlled group left within the last 5 years. (PBGC can file claims against them); and
(e) whether there are any Due and Unpaid Employer Contributions (DUEC's). This would include the balances of waivers that come due on DOPT, per 4062(c).

(4) Administration of Plan During Pendency of Distress Termination Proceedings. After the NOIT and until the PBGC makes its determination in (5) below, the plan administrator must refrain from paying lump sums (except death benefits), making loans, or purchasing irrevocable commitments from insurers – §4041.42. After the proposed DOPT, only guaranteed benefits (or benefits allocated under §4044) are payable. The plan sponsor and actuary should contact the PBGC actuaries to make these benefit cutbacks. If the termination is not approved, these cutbacks must be restored with interest.

(5) PBGC Review The PBGC will notify the plan administrator of its determination whether Distress criteria have been met as soon as possible (not limited to 60 days by law or regulation) and the plan administrator is to carry out item (6).

(6) Distribution or Trusteeship by PBGC

(a) If assets are sufficient for all benefit liabilities, the plan administrator must terminate the plan under standard termination procedures. A standard termination is often considerably faster and less costly for a plan, due to PBGC's more conservative assumptions, and prohibition from paying lump sums.
(b) If assets are not sufficient for all benefit liabilities, but they are sufficient for guaranteed benefits, the plan administrator must distribute available assets under procedures similar to a standard termination. Important Note: In order for a plan's assets to be sufficient for guaranteed benefits, they must also cover all non-guaranteed benefits in priority categories 1 through 4 (defined in Chapter VII). The PBGC will not become trustee of the plan. Instead PBGC will file a claim for the employee's outstanding benefit liabilities, collect them and pay them out per §4022(c) - as discussed in Chapter VII.
(c) If assets are insufficient for guaranteed benefits, the PBGC will trustee the full plan. In such cases, the plan administrator must submit the name, address, all plan documents, actuarial valuations, government filings, trust information, employee data, benefit calculations/amounts, and present values (using §4044(b)) for each participant so that the PBGC can administer the terminated plan. This detailed information is not needed until the later of 120 days after the proposed DOPT, or 30 days after receipt of PBGC's determination that the requirements for distress termination are satisfied.

(7) Notice of Benefit Distribution Within 60 days after the PBGC confirms that the plan is sufficient for guaranteed benefits (items 6a and 6b above), the P/A must send a notice to each affected party (other

than PBGC and union), providing: (a) information on how much of their plan benefits they will receive, and (b) information about the insurer (at least 45 days before distribution).

(8) Form 602: Post-Distribution Certification must be received by the PBGC within 30 days after distributions in (6)(a) and (b) above.

Other Issues For Distress Terminations

In case their Distress Termination filing fails, some practitioners also file for a Standard Termination (and promise to make the plan sufficient for all benefit liabilities) to keep their proposed DOPT. If the Distress Termination fails due to an incomplete filing, the plan administrator has 30 days after notification to complete the filing correctly. The PBGC, on its own initiative, may waive certain rules and deadlines if it is in the PBGC's interests. Otherwise, the proposed termination fails and the P/A must notify all affected parties.

The PBGC has a couple of interesting powers that strengthen its hand after Distress Terminations occur:

(1) §4045 allows the PBGC to recapture portions of large payments to participants in the 3 years leading up to DOPT. The amount recaptured is the payments made in excess of (1) the life annuity benefit amount which the participant would have received over (2) $10,000 per year. You can see it is meant to recapture portions of large benefits paid out in lump sums or in period-certain annuities.

(2) §4047 allows the PBGC to restore pension plans back to their plan sponsor if consistent with PBGC's purpose - see §4002(a). In June of 1990, the Supreme Court upheld this right by overturning lower court decisions and allowing LTV's plans to be restored, because LTV had abused the PBGC's pension insurance system by creating follow-on plans which basically made up for participant's benefit cutbacks made by the PBGC. LTV was indirectly using PBGC as its funding mechanism of its old plan.

Under PBGC v. LTV, 110 Supreme Court 2668 (1990), the PBGC was not required to consider principles and policies of bankruptcy law. (Id. at 2676) or to find that the employer's financial condition had improved (Id. at 2678) in determining whether to restore a terminated pension plan. The law allows the agency to restore whenever "restoration would further the interests of Title IV of ERISA" (Id. at 2675,6).

Upon restoration, Treasury regulation 1.412(c)(1)-3 allows the PBGC to set up the amortization period for the plan's initial restoration amortization base (not to exceed 30 years), annually review the plans funding, and modify the amortization payments as necessary. This helps employers, such as LTV, meet their minimum funding requirements after restoration.

3. Accessing Plan Assets

Currently, plan assets cannot be withdrawn (diverted to any other purpose other than the exclusive benefit of participants and beneficiaries) "prior to the satisfaction of all liabilities" per §401(a)(2), except through transferring certain funds from well funded plans to a §401(h) retiree health account as per IRC §420. The IRS allows recapture of surplus assets from a defined benefit plan only upon complete termination per 1.401-2(b)(1). For this reason, in the past many plan sponsors would terminate their plans, purchase accrued benefits for everyone, take the surplus, and re-establish the same plan with an offset of the purchased annuities (termination-reestablishment). Another alternative is to spinoff actives, terminate the retiree plan, purchase their annuities, and take the surplus (spinoff-termination). This does not happen much anymore because the excise tax on reversions (on top of income tax) is so high.

Using "form over substance", some felt this these two-step processes were "shams" since the employer got the reversion without having to comply with the termination rules, which would have required vesting of everyone per §411(d)(3) and annuitizing everyone because of §401(a)(2). The PBGC was also unhappy because now it had to guarantee benefits in a plan with no surplus cushion. Thus, the Administration's "Joint Implementation Guidelines" (see Appendix B) were created in May of 1984. In order to obtain favorable determinations from the IRS & PBGC, a plan must meet the following criteria:

- All participants and beneficiaries in the original plan must be given advance notice of this transaction as if the entire original plan were being terminated. PBGC Regulation §4041.23(c) says participants in **the** ongoing plan of a spinoff should be given this notice when the NOIT goes out to the terminating plan.
- The plans must vest everyone 100%.
- The plans must annuitize everyone.
- Under termination-reestablishment, the new plan's unfunded liability must be amortized over the weighted average future working lifetime if less than 30.
- Under spinoff-termination, amortization bases must be combined and offset.
- It cannot happen again for 15 years.

In 1987, the Reagan Administration proposed a bill which would have allowed withdrawals of excess assets from a plan if an asset margin remained in the plan over termination liabilities. Congress did not include this in OBRA87 and thus the Joint Implementation Guidelines are still in effect.

Another way to utilize surplus assets in a pension plan is to merge it with an underfunded plan. The underfunded plan's participants will appreciate that and so will the PBGC, but maybe not so with the participants in the overfunded plan. When the overfunded Gulf plan was merged into the Chevron plan (when Chevron bought Gulf), Gulf employees brought a class action suit against Chevron, as they said the Gulf plan never said the employer was entitled to the surplus. Chevron says they did not terminate the plan, nor did they do anything illegal. The U.S. District Court in Houston agreed with the employer.

Also, see the section on Reversions in this chapter for other ways to use pension surplus.
For related information on withdrawing assets from a pension plan, see Chapter VII, sections 6 and 9.

4. Termination and Coverage Statistics

The PBGC insurance programs protect approximately 44 million American workers and retirees in about 31,000 private defined benefit pension plans. In 2004, the PBGC took on benefit responsibility for 147,000 new participants, so that they are now responsible for the benefits of over 1 million people. Though the number of new participants was a smaller number than in 2002 and 2003, it was still the third highest year ever, and well above historical rates. The 2004 PBGC financials show a deficit of $23 billion and reasonably possible liabilities of almost another $100 billion from bankrupt airlines, auto parts

companies, and other entities in below investment grade status. There will likely be significant changes in the funding rules for defined benefit pension plans over the next few years, and an increase in PBGC's premiums.

Annual reports on the PBGC program are available back to 1995 at www.pbgc.gov/workers-retirees/index.html. Click on the link for annual reports. This link will give you the most up-to-date status of the PBGC programs and coverage.

IV. BASIC-TYPE BENEFITS

The law allows the PBGC some discretion in defining what benefits from a pension plan are basic-type benefits and thus guaranteeable. Committee Reports for Section 4001 (definitions) suggest that non-basic benefits may include supplemental benefits and ancillary benefits (such as benefits payable upon death or disablement after plan termination).

There is an important distinction to be noted here between Basic-type Benefits (or Guaranteeable Benefits) and Basic Benefits (or Guaranteed Benefits). A Basic-type Benefit is a type of benefit that would be guaranteed by the PBGC except for the maximum and phase-in limitations placed on guaranteed (basic) benefits. For example, a level benefit of $4,000 per month payable for life is a guaranteeable benefit, but is not a guaranteed benefit. Only the portions of the guaranteeable benefit under the maximum (defined in the next chapter) are guaranteed.

In order for a benefit to qualify as a Basic-type Benefit (Guaranteeable Benefit) it must satisfy the requirements set forth in the "Guaranteed Benefits" regulation 4022, Subpart A. There are four criteria which are set forth in this regulation. They are:
A) Benefit must be non-forfeitable on date of plan termination (DOPT) under 4022.5,
B) Benefit must be a pension benefit as defined in 4022.2,
C) Participant must be entitled to the benefit under 4022.4, and
D) Benefit must not exceed the accrued benefit at normal retirement age in a single life form: 4022.21.

A non-forfeitable benefit (Criteria A), also defined in law in §4001(a)(8), is a benefit for which a participant has satisfied all the conditions for entitlement under the plan (or ERISA if the plan has not been "ERISAfied"), other than:

- Submission of a formal application,
- Retirement,
- Completion of a required waiting period (for disability, etc.), or
- Death in the case of a return of employee contributions.

Benefits that become non-forfeitable solely on termination or partial termination of the plan are considered forfeitable for both guarantee purposes and allocation purposes.

A pension benefit (Criteria B) is a benefit payable as an annuity (fixed or contingent period) to a participant who permanently leaves (or has permanently left) covered employment, or to a beneficiary, which provides a substantially level income to the recipient. The effect of these rules on various benefits is as follows:

- Social Security Leveling Options are deemed to be pension benefits even though not level, because they provide a substantially level income in combination with Social Security that is actuarially equivalent to the level accrued benefit in normal form.
- The PBGC does not guarantee benefits to participants who continue working at the same facility (even though there is a new owner) because the participant has not permanently left covered employment. When they retire, the PBGC will pay a benefit. It will be interesting to see what PBGC does if and when IRS finalizes a regulation allowing the payment of partial pension benefits for qualifying phased retirement programs.
- The PBGC does not guarantee lump sums, because they do not provide a level income.
- An important exception to these criteria relates to plans that require employee contributions. In April 1978 this regulation was revised to provide that the refund of mandatory contributions upon the death of a participant would qualify as a basic-type benefit even though it is not a pension benefit.

Entitlement (Criteria C): Participants in pay-status on the date of plan termination (DOPT) are entitled to their pay-status benefit. Non-pay-status participants are entitled to the automatic form of annuity payable based on their marital status at the date of plan termination. This has the following affect:

- The PBGC will honor optional forms elected before DOPT (i.e. they are entitled to the form).
- A subsidized optional form (for example, a subsidized J&100% S option) is not guaranteeable because the non-pay-status participant is not entitled to it (unless elected prior to DOPT). This caused problems for people whose marital status changed before their benefit commencement date. So in 1986, the PBGC administratively decided to pay benefits based on the marital status as of benefit commencement date (except that the subsidized portion of the automatic QJSA benefit, if any, will not be paid to those who were single on DOPT, unless covered by assets in Priority Categories 5 or 6).

Criteria D merits some elaboration. In PBGC's proposed regulation 2605 (later 2613 and now 4022), no part of a supplemental pension was to be guaranteeable. However, commentators objected to this because there is only a very fine semantic distinction between an unreduced early retirement benefit and the part of the supplemental benefit that is less than the normal retirement benefit. Thus, the final regulation 4022.21 provides that the portion of the total benefit that exceeds the dollar amount of the accrued benefit payable as a straight life annuity commencing at normal retirement will not be guaranteeable. An example with graph follows:

1.	Normal Retirement Age (NRA)	65
2.	Actual Retirement Age (ARA)	55
3.	Accrued Benefit at NRA	$1,000
4.	Early Retirement Reduction Factor at ARA	60%
5.	Lifetime Benefit Payable at ARA = (3) x (4)	$600
6.	Supplement Payable from ARA to 62	$500
7.	Total Plan Benefit Payable from ARA to 62 = (5)+(6)	$1,100
8.	Portion Guaranteed □(3)	$1,000
9.	Portion of Supplement Not Guaranteed = (7) - (8)	$100
10.	Guaranteed Benefit after 62 = (5)	$600

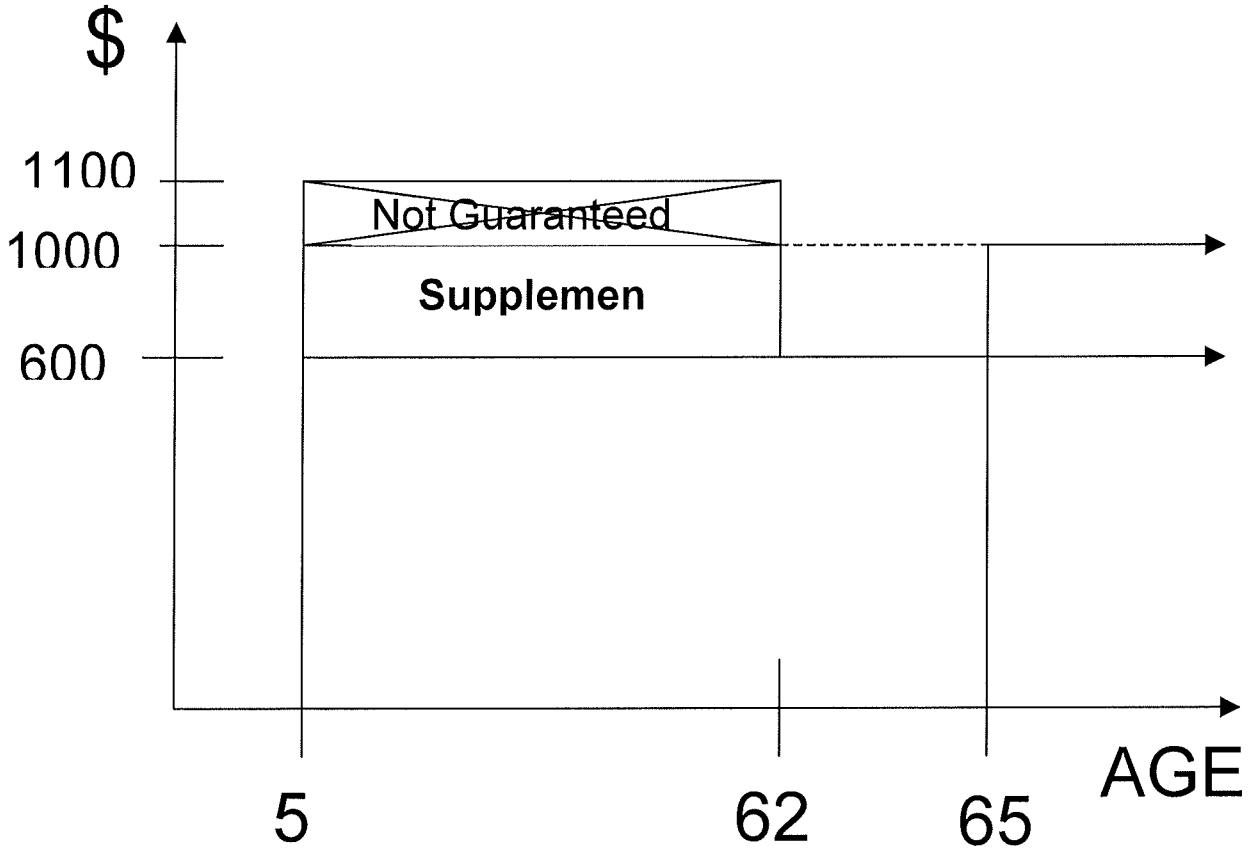
Since each of the installments payable prior to age 62 exceeds the accrued benefit of $1000 per month commencing at normal retirement, only the first $1000 of each installment would satisfy this limitation. Note that this benefit would not satisfy the 4022.21(a)(2)(iii) exemption that makes the Social Security Leveling Option found in many plans guaranteeable. Because the 60% Early Retirement Reduction Factor in the example approximates an actuarial reduction, the $500 supplement increases the value of the early retirement pension beyond the value of the accrued normal retirement benefit. Now suppose the person above chooses a J&S benefit. They can get their full benefit guaranteed if it is less than $1,000 in total, as follows:

11.	J&S Factor	80%
12.	J&S Lifetime Benefit (5) x (11)	$480
13.	Total Benefit (6) + (12)	$980
14.	Guaranteed Benefit □ (3)	$980 (Fully Guaranteed!)

The full disability pension in pay status on DOPT is also considered basic-type. Thus, even though it may be greater than the accrued benefit at NRA (by using service projected to NRA), it will be guaranteed, subject to the maximum and phase-in rules on the following pages. See 4022.21(a)(2)(ii).

Guaranteed benefits (or basic benefits) are benefits guaranteeable under Part 4022 by the PBGC, but limited to a maximum and also further reduced for recent benefit increases. Details are provided in the next chapter.

Nothing in Excess of the Accrued Benefit Payable at



V. GUARANTEED BENEFITS

While Congress was not specific on what type of benefits were to be guaranteeable, it was very specific on what amounts were to be guaranteed. In Section 4022, Congress limits guaranteed benefits to protect the insurance program from benefits that could abuse it such as (1) very large benefit amounts and (2) amendments increasing benefits just before termination. Pension plans are allowed to fund benefit increases over many years, so Congress let the PBGC phase-in benefit improvements over 5 years and benefits for substantial owners (the ones who make funding decisions) over 30 years (30 is the number of years over which a benefit increase could be funded in the original ERISA). The following pages discuss the specifics of these limitations.

1. Maximum Guaranteeable Benefit

ERISA Section 4022(b)(3) limits the value of guaranteed benefits to the actuarial value of a life annuity commencing at age 65 equal to the lesser of:

(1) 100% of a participant's highest 5 year average income or
(2) $750 indexed in accordance with the Social Security Taxable Wage Base. The indexation of the $750 can be found in PBGC regulation § 4022 Appendix D and is developed by the table on the next page.

As shown in the examples three pages later, the maximum is reduced if benefits are received in a different form or if they commence before age 65. If the participant is already retired on DOPT, the age on DOPT is used, not the age when they retired. A table of factors used to reduce the maximum is two pages after this one. For example, if DOPT is 2005, the participant is age 60, the form is J&50%S (contingent) with 10 years certain, and the spouse is age 57, the PBGC maximum is:

$3,801.14 x .65 x.90 x .96 x .97 = $2,070.68

The maximum insurance limit for certain period annuities (no life contingent benefit) is the actuarial equivalent of the life annuity at the same age using the UP84 table (unisex version) and interest rates in effect on plan termination. This is commonly needed when a spouse is receiving a remaining period certain benefit from the retiree's certain and life benefit.

Due to the Retirement Protection Act of 1994, participants that are disabled using Social Security's definition, do not have any reductions to the maximum on account of age. When a disabled participant receiving a J&50%S dies, the surviving spouse will receive 50% of the benefit they were receiving. There will be no adjustment to the age 65 maximum, just because the surviving spouse is not disabled.

PBGC Maximum Guaranteeable Benefit

Yr. of Plan Termination	(1) Social Security Wage Base	(2) Wage Base used to Compute Maximum	(3) Monthly SLA Limit @ 65 750x(2)/13,200	(4) Annual SLA Limit @ 65 (3) x 12
1974	$13,200	$13,200	$750.00	$9,000.00
1975	14,100	14,100	$801.14	$9,613.68
1976	15,300	15,300	$869.32	$10,431.84
1977	16,500	16,500	$937.50	$11,250.00
1978	17,700	17,700	$1,005.68	$12,068.16
1979	22,900	18,900	$1,073.86	$12,886.32
...	...	...	...	...
2001	80,400	59,700	$3,392.05	$40,704.60
2002	84,900	63,000	$3,579.55	$42,954.60
2003	87,000	64,500	$3,664.77	$43,977.24
2004	87,900	65,100	$3,698.86	$44386.32
2005	90,000	66,900	$3,801.14	$45,613.68
2006	94,200	69,900	$3,971.59	$47,659.08

The $3,801.14 maximum will be used instead of $750 for every participant in a plan that terminated in 2005, whether they are in pay-status on the date of plan termination or are very young and will not begin payments for many years. The maximum amount at age 65 changes every January 1 that the SSA wage base changes. The 1977 Amendments to the Social Security Act increased the Social Security Maximum Taxable Wage Base in an ad hoc manner by more than the indexation would have. However, the PBGC maximum guaranteeable benefit is still computed as if the 1977 Amendments were not passed. For example, since the Maximum Taxable Wage Base would have been $18,900 in 1979 under the Social Security Act before it was amended in 1977, the 1979 Maximum Guaranteeable Benefit is $1,073.86 ($750.00 x $18,900 / $13,200).

Factors Used to Reduce Maximum
if payable other than a SLA @ 65 (29 CFR 4022.21ff)

Form			Age		Age Difference for J&S Beneficiary		
Form		Factor	Age*	Factor	Difference	Younger	Older
Straight Life		1.000	65 & over	1.0	1	.99	1.005
C&C *			64	.93	2	.98	1.010
1		.995	63	.86	3	.97	1.015
2		.990	62	.79	4	.96	1.020
3		.985	61	.72	5	.95	1.025
4		.980	60	.65	6	.94	1.030
5		.975	59	.61	7	.93	1.035
6		.965	58	.57	8	.92	1.040
7		.955	57	.53	9	.91	1.045
8		.945	56	.49	10	.90	1.050
9		.935	55	.45	11	.89	1.055
10		.925	54	.43	12	.88	1.060
Reduction decreases by .01 per year for each year in excess of 10			53	.41	13	.87	1.065
			52	.39	14	.86	1.070
			51	.37	15	.85	1.075
			50	.35	16	.84	1.080
			49	.33	17	.83	1.085
J&S (contingent) #		w/10c&c	48	.31	18	.82	1.090
50%	.90	x .960	47	.29	19	.81	1.095
66-2/3%	.8667	x .970	46	.27	20	.80	1.100
75%	.85	x .975	45	.25			
100%	.80	x .990					
			* Interpolate between whole years for monthly factors		When beneficiary is older, conversion factor increases 1/4% per year for ages in excess of 20 yrs. When beneficiary is younger, conversion factor decreases 1/2% per year in excess of 20 yrs.		
J&S (joint) #							
50%	1.00						
66-2/3%	.93						
75%	.90		# Interpolate for other % continuation				
100%	.80						

Limit ages to 65 for employee and/or spouse when calculating the maximum. We understand that PBGC may be applying Late Retirement Factors greater than one for certain participants who are over age 65.

Age reductions do not apply to disability benefits for participants receiving Social Security disability benefits (effective for Notices of Intent to Terminate after 12/8/94 due to RPA94).

The exact operation of these limits is set forth in the "Limitation on Guaranteed Benefits" regulation. (Title 29 - Labor; Chapter XL - PBGC; Part 4022). While the actual operation of the adjustment factors set forth in 4041 Subpart B are relatively straight-forward, a few examples may be helpful.

Sample Maximum Calculations

	Case #1	Case #2	Case #3
Year of Plan Termination	1974	1976	1978
Retirement Age or Recipient's Age at Plan Termination if in pay status[8]	65	65	60
Form of Benefit at Plan Termination:	Life Annuity	10yr C&C	10yr C&C
Highest 5-Year Average Monthly Income Calculation of Maximum Limitation:	$1,000.00	$1,000.00	$1,000.00
1) $750 Indexed to Yr. of Plan Termination	$ 750	$ 869.32	$1,005.68
2) Lesser of (1) and High 5 Monthly Income	$ 750	$ 869.32	$1,000.00
3) PBGC Actuarial Age Adjustment Factor	1.000	1.000	.650
4) PBGC Actuarial Form Adjustment Factor	1.000	.925	.925
5) Maximum Limitation:(2)x(3)x(4)	$ 750	$ 804.12	$ 601.25

Suppose under Case #1 above that the plan allows benefits to commence at any time between ages 55 and 70. Under these circumstances the maximum guaranteeable benefit would range from .45 x $750 or $337.50 (if the participant retires at age 55) to $750.00 (if the participant retires at or after age 65.)

Suppose in Case #3 above the retiree retired 3 years before DOPT, so that the form at DOPT is just 7 C&C to the PBGC. Then the 10C&C factor of .925 would not be used. The 7 C&C factor of 0.955 would be used per 4022.23(d)(1). Since the retiree is age 63 on DOPT, the age factor would be 0.86 per 4022.23(c). Thus, one should use the age and form on DOPT for those already receiving benefits on DOPT. If in the above case the retiree is dead, the form is a 7-year certain annuity.

Suppose under Case #3 above that the form of benefit at DOPT is J&50%S (contingent) and the spouse is four years younger then the employee. Then the PBGC form adjustment factor (line 4) is .90 x .96 = .8640 and the maximum benefit is a $561.60 J&50%S.

Note: The J&X%S benefit of a survivor who goes into pay status before DOPT can be equal to the maximum, but if the survivor goes into pay status after DOPT, then the participant's benefit is limited to the maximum and the survivor only gets X% of the participant's maximum.

[8] Use a maximum age of 65. Note: if spouse is a recipient, use spouse's age at DOPT (with a maximum of 65). We understand that PBGC may apply late retirement factors greater than 1 above age 65.

2. Phase-In of Benefit Increases for Participants other than Substantial Owners

Benefits in effect less than 5 years prior to the date of plan termination (DOPT) are not fully guaranteed (unless small). In fact, a benefit increase (or plan) is not guaranteed at all if the effective date is less than 1 full year prior to DOPT. The 5-year phase-in rule phases in 20% of 1-year-old increases (or at least the first $20), 40% of 2 year old increases (or at least the first $40), etc. For example, a $200 benefit increase in effect for 3 full years would have $120 guaranteed (60% of $200). If the benefit increase had been only $80, then $60 would be guaranteed (as $60 is greater than 60% of $80). The full increase would be guaranteed if it was $60 or less. The flat dollar phase-ins (e.g., $20) are irrespective of the form. Thus, the $20 phase-in is better for people who select J&S forms and those who retire early.

A re-established plan with substantially the same benefits is a continuation of the prior plan for purposes of counting the number of years that the benefits have been in effect.

Determining Years in Effect: The date on which the amendment (or plan) is adopted is used if later than the effective date (thus eliminating abusive retroactive effective dates). An amendment with future scheduled benefit increases or future COLA's will have the future increases phased-in from their scheduled dates. If a plan amendment's adoption or adopted date is in question, then the employer's signature and date on a collective bargaining agreement or board meeting minutes indicating that the trust is paying amended benefit amounts can be used. Post-SEPPA, one must determine the number of full years the benefit increase was in effect "beginning with that date". Prior to SEPPA (eff. 1/1/86), the words were "following that date". Thus, a benefit in effect on 5/1/86 for a plan with a DOPT of 4/30/87 is 20% phased-in. A similar situation prior to SEPPA would have meant no PBGC guarantee. If, during the five-year period prior to DOPT, two amendments fall within the same year measured from DOPT, the later plan provisions are used (See example 10 in Appendix A).

Normalization of Form (to Final Form of Benefit): If an amendment changes the form of the benefit or makes the vested benefit available earlier, the older plan benefit is converted to the most recent plan's form (a.k.a. final form) using the older plan factors where available (as extended by PBGC actuarial equivalent factors, if needed). This conversion (known as "Normalization") is necessary, as otherwise there would be no way of determining the amount of the benefit increase to be phased-in. If an amendment changes the entitlement provisions (including employer consent), then impute the later entitlement provisions to the vested benefit in the older plan (do not phase-in from zero). Sometimes you do phase in from $0 – or example, if the vesting percent went from 0% to 100%.

The exact procedures to be followed in computing the guaranteed portion of a benefit for participants other than substantial owners are described in 4022.24 and 2621.25. A few illustrations may be helpful. A blank computation worksheet has also been attached for your future use, if needed.

Sample Phase-In Calculations

	Case #1	Case #2	Case #3
Date of Plan Termination (DOPT)	5/1/87	10/5/77	1/30/76
Age of Participant @ DOPT	65	45	Spouse
Beneficiary Age 63			
Age of Participant @ Retirement	62	65	65
Benefit Under Amended Plan:			
a. Amount (monthly)	$425.00	$950.00	$250.00 to
beneficiary			
b. Form	10yrC&C	Single Life	J&50%S
(contingent)			
c. NRA 62	65	65	
Benefit Before Amendment:			
a. Amount (monthly) @ NRA	$425.00	$800.00	$510.00 to
participant			
b. Form Single Life	10yr C&C	Single Life	
c. NRA 65	65	65	
d. Early Retirement Reduction	6%/yr.	N/A	N/A
e. J&S Plan Conversion Factor	N/A	N/A	.873
Years from Amendment to DOPT	4	4	2
High 5 (monthly)	4,000	1,200	1,000
Calculation of Maximum Guaranteed Benefit:			
1. Maximum Life Annuity at 65	$1,857.95	$ 937.50	$ 869.32
2. Age Adjustment Factor	1.000	1.000	.860
3. Form Adjustment Factor	.955	1.000	1.000
4. Maximum (1) x (2) x (3)	$1,774.34	$ 937.50	$ 747.62

Case #1

Case #1 illustrates "normalization" for a pensioner whose plan was amended before he retired to increase benefits. In Case #1, the early retirement reduction @ 62 was eliminated when the Normal Retirement Age changed from 65 to 62 and the form of benefit was changed from a life annuity to a 10 C&C annuity. Thus, we multiply the single life annuity at age 65 of $425 by .925 (to convert what the benefit amount would have been if payable as a 10 C&C) and by .82 (the early retirement reduction factor, assuming the participant had retired at age 62 under the former plan). Useplan factors when available otherwise use PBGC factors.

Case #2

Case #2 illustrates several points regarding the phase-in:

(1) The guaranteeable benefit increase is the increase up to the maximum guaranteed benefit only, not the total benefit increase (i.e., do not phase-in any portion of the benefit in excess of the maximum).
(2) The $80 maximum phase-in is not adjusted for form of benefit or age of benefit commencement. (A result of not adjusting the dollar amount phase-in for form or age is that proportionately more of a benefit can be phased-in at younger ages and more costly forms such as J&S and 10 C&C. In fact, many times a benefit can be fully phased-in at age 55, but not at age 65).
(3) The phased-in increase in column (6) cannot be greater than the increase subject to phase-in from column (5).

Case #3

Case #3 illustrates the adjustment set forth in 4022.24(c)(4). This paragraph required that the benefit payable under the terms of the plan prior to the increase after having been adjusted to reflect the change in age and/or form of payment must be further adjusted to determine the amount which would be payable if the **conditions existing at the date of termination had existed on the date of increase.** For example, consider a survivor benefit which was not payable as of the date the plan was amended but which became payable subsequently upon the death of a participant. Case #3 is such a situation. As of the date of plan termination the participant had died and the beneficiary was receiving the spousal benefit. As of the date the plan was amended the participant was active. The plan's J&S factor of .873 was used because that is what the old plan would have specified the spouse's benefit to be based on. One then multiplies by 1/2 to arrive at the benefit, because that reflects the conditions in effect on DOPT. For maximum benefit purposes, however, the age adjustment factor is .860 and the form adjustment factor is 1.00 (because they **reflect the age of the beneficiary and form on DOPT**, i.e., the age and form when the PBGC becomes responsible for the liabilities).

When you have to do a phase-in on a J&S benefit where the spouse died before DOPT, §4022.24(c)(2) states that you treat it as a life only benefit.

Worksheet Instructions

Column

(1) Working from the bottom row and up, list the date of plan termination and the five previous years leading to it.

(2) Determine the benefit amount and form that the participant would be entitled to, if he or she had terminated employment on DOPT (date of plan termination) ignoring any plan amendments subsequent to the corresponding date in column (1).

(3) Using the Benefit Conversion Worksheet, convert each benefit in column (2) to its "equivalent amount" based on final form plan provisions.

(4) Compute the maximum guaranteeable benefit based on final form provisions.

(5) Copy over all amounts in column (3) that are less than (4). For amounts in column (3) greater than (4), copy over the figure in (4).

(6) From column (5), subtract row 1 from row 2, row 2 from row 3, and so on.

(7) Compare the amount in column (6) to its corresponding $X - X% "phase in rule".
   a. if the amount is greater than $100 multiply it by X%
   b. if the amount is less than $100,
      (i) but greater than $X, copy over $X
      (ii) and less than $X, copy over the amount.

(8) Add all the rows in column (7) to arrive at the PBGC guaranteed benefit.

Examples of Worksheet

A. Background:
   1. ABC Company Pension Plan Termination 7/20/88
   2. Participant Data
      a. John Doe, age 60, 30 years of credited service, spouse age 50.
      b. Jim Jones, age 40, 10 years of credited service, spouse age 42.

B. Summary of Plan Provisions
   1. Provisions in effect 5 years prior to plan termination (7/20/83)

      NRB: $25 x years of credited service
      NRA: age 65
      Form: straight life annuity
      Vesting: 25% after 5 years of service, increasing at 5% per year to 10 years of service, then increasing 10% per year thereafter to 100% after 15 years.
      Plan Factors: Same as PBGC

   2. Subsequent Amendments

Date	Amendments
8/1/83	$25 increased to $30
5/1/84	normal form: 10 C&C
10/1/84	$30 increased to $35
8/1/85	normal retirement age now 60
9/1/85	10 year cliff vesting
5/1/87	$35 increased to $40
5/1/88	normal form is now 75% J&S contingent

PHASE-IN COMPUTATION WORKSHEET

Name:_____

DOB: _____ NRD: _____ ARA: _____

DOTE: _____ ERD: _____

DOH: _____ DOPT: _____

CS: _____ AGE: _____

(6) Maximum Guaranteeable Benefit

= $ $Limit_{DOPT}$ x AgeFactor x FormFactor

= _____

= _____

(1) PLAN BENEFIT PROVISIONS	(2) YEARS IN EFFECT	(3) MONTHLY BENEFIT UNDER THE PLAN	(4) NORMALIZATION	(5) BENEFIT CONVERTED TO FINAL FORM	(6) LIMITED TO MAXIMUM GUARANTEEABLE LIMITATION	(7) INCREASE SUBJECT TO PHASE-IN	Phase-In	(8) PHASED-IN INCREASE
	5+						100%	
	4						$80-80%	
	3						$60-60%	
	2						$40-40%	
	1						$20-20%	
	0						$ 0- 0%	

Years in Effect: Count endpoints. 5/10/96 to 5/9/97 is a full year.
Count years in prior plan, if this is a successor plan
Use latest of Effective Date, Adopted Date, and Scheduled Effective Date

(8) PBGC GUARANTEED BENEFIT _____

Benefit Increases also include: liberalized vesting, entitlement, participation, and earlier retirement

For MAXIMUM: Dollar Limit is as of DOPT; Age factor uses ARA (or age at DOPT if later), but ⇑ 65
Form Factor for a retiree is determined from form at DOPT. Thus, in a J&S, if employee or spouse dies before DOPT, then benefit form is Life Only. For example, in J&50%S, if employee dies after DOPT, spouse gets 50% of Maximum; if employee dies before DOPT, spouse gets full Maximum.

Benefit Conversion

Participant	Old Benefit	Plan Factors	New Benefit in Final Form
John Doe	$ 750 straight life at 65	(.85) (.65) (.9)/(1) (1) (1)	= **$ 372.94**
	900 10 C&C at 65	(.85) (.65) (.9)/(.925) (1) (1)	= **483.82**
	1,050 10 C&C at 65	(.85) (.65) (.9)/(.925) (1) (1)	= **564.44**
	1,050 10 C&C at 60	(.85) (.65) (.9)/(.925) (.65) (1)	= **868.37**
	1,200 10 C&C at 60	(.85) (.65) (.9)/(.925) (.65) (1)	= **992.42**
	1,200 75% J&S at 60	(.85) (.65) (.9)/(.85) (.65) (.9)	= **1,200.00**
Maximum Guaranteeable Benefit		*PBGC Factors*	
	1,909.09 straight life at 65	(.85) (.65) (.9)/(1) (1) (1)	= **949.30**

Participant	Old Benefit	Plan Factors	New Benefit in Final Form
Jim Jones	$125 straight life at 65	(.85) (.65) (1.01)/(1) (1) (1)	= **$ 69.75**
	150 10 C&C at 65	(.85) (.65) (1.01)/(.925) (1) (1)	= **90.49**
	175 10 C&C at 65	(.85) (.65) (1.01)/(.925) (1) (1)	= **105.57**
	350 10 C&C at 60	(.85) (.65) (1.01)/(.925) (.65) (1)	= **324.84**
	400 10 C&C at 60	(.85) (.65) (1.01)/(.925) (.65) (1)	= **371.24**
	400 75% J&S at 60	(.85) (.65) (1.01)/(.85) (.65) (1.01)	= **400.00**
Maximum Guaranteeable Benefit		*PBGC factors*	
	1,909.09 straight life at 65	(.85) (.65) (1.01)/(1) (1) (1)	= **1,065.31**

PHASE-IN COMPUTATION WORKSHEET

John Doe, age 60, 30 years of credited service, spouse age 50.

(4) Maximum Guaranteeable Benefit $1909.09 --> $949.30

(1) PLAN BENEFIT Provision	(2) YEARS IN EFFECT	(3) MONTHLY BENEFIT UNDER THE PLAN	(4) Normalization	(5) BENEFIT CONVERTED TO FINAL FORM 75% J&S @ 60	(6) Maximum Guaranteeable LIMITATION	(7) INCREASE SUBJECT TO PHASE-IN	Phase-In	(8) PHASED-IN INCREASE
7/20/83	5	$750 SLA, 65		$372.94	$372.94			$372.94
7/20/84	4	900 10C&C, 65		483.82	483.82	110.88	$80/80%	88.70
7/20/85	3	1050 10C&C, 65		564.44	564.44	80.62	$60-60%	60.00
7/20/86	2	1050 10C&C, 60		868.37	868.37	303.93	$40-40%	121.57
7/20/87	1	1200 10C&C, 60		992.42	949.30	80.93	$20-20%	20.00
7/20/88	0	1200 75%J&S, 60		1,200	949.30	0	$ 0- 0%	0.00

(8) PBGC GUARANTEED BENEFIT $ 663.21

PHASE-IN COMPUTATION WORKSHEET

Jim Jones, age 40, 10 years of credited service, spouse age 42.

(4) Maximum Guaranteeable Benefit $1909.09 --> $1065.31

(1) PLAN BENEFIT Provision	(2) YEARS IN EFFECT	(3) MONTHLY BENEFIT UNDER THE PLAN	(4) Normalization	(5) BENEFIT CONVERTED TO FINAL FORM 75% J&S @ 60	(6) Maximum Guaranteeable LIMITATION	(7) INCREASE SUBJECT TO PHASE-IN	Phase-In	(8) PHASED-IN INCREASE
7/20/83	5	125 SLA, 65		$ 69.75	$ 69.75			$ 69.75
7/20/84	4	150 10C&C, 65		90.49	90.49	20.74	$80/80%	20.74
7/20/85	3	175 10C&C, 65		105.57	105.57	15.08	$60-60%	15.08
7/20/86	2	350 10C&C, 60		324.84	324.84	219.27	$40-40%	87.71
7/20/87	1	400 10C&C, 60		371.24	371.24	46.40	$20-20%	20.00
7/20/88	0	400 75%J&S, 60		400.00	400.00	28.76	$ 0- 0%	0
		(8) PBGC GUARANTEED BENEFIT						$ 213.28

3. Phase-In of Benefit Increases for Substantial Owners

ERISA Section 4022(b)(5) places a special limitation on the guaranteed benefits for substantial owners (generally 10% ownership). The special 30-year phase-in rules are set forth in 4022.26. Special note should be made of the last sentence of 4022(b)(5) which limits the total guaranteed benefit for substantial owners to 200% of the amount guaranteed based on the 30-year phase-in under the oldest plan under which the substantial owner participated. PBGC has interpreted this to cause a severe cut back as can be seen from the following example:

Substantial Owner Calculation
Plan Inception = 1/1/62
Service = 30 Years
DOPT = 1/1/87

Date	Benefit As of Date	SLA @ 65	Phase-In	P/I[9]	Amount Phased-In
1) 25 yrs ago[10]	$10 X Svc	$300	$300	25/30	$250.00
2) 20 yrs ago	25 X Svc	750	450	20/30	300.00
3) 10 yrs ago	50 X Svc	1500	750	10/30	250.00
4) 1 yr ago	100 X Svc	3,000	357.95[11]	1/30	11.93
5) Sum of (2), (3), and (4)					561.93
6) Maximum Allowable Increase - limit Item (5) to Item (1)					250.00
7) Guaranteed Benefit - Item (1) plus Item (6)					500.00

In fact, if the plan at inception did not have a guaranteeable benefit (say, if the benefit did not vest until NRD) then the substantial owner's guaranteed benefit would equal 200% of $0 or $0. Note that this is only onerous if the plan was poorly funded. If the plan were well funded (by the substantial owner), then he/she would receive a benefit from the asset allocation, which is discussed later. A substantial owner (S/O) is defined in Section 4022(b)(5) as anyone who owns at least 10% of the entity within the 60 months prior to DOPT. If the S/O was not always a S/O, compute the benefit under both S/O and non-S/O methods. The guaranteed benefit is a pro-ration of those 2 amounts using participation service while in each status. (Note: do not count service while plan was not in effect.) For example:

Partial S/O Calculation

Guaranteed Benefit if always an S/O	$100
Guaranteed Benefit if never an S/O	$200
Years as an S/O	5.5
Years not an S/O	4.5

Guaranteed Benefit = (5.5/10) x 100 + (4.5/10) x 200 = $145.

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[9] Numerator of Phase-In fraction is limited to years in which S/O was an active participant. Use only full years.

[10] Plan Inception

[11] The benefit is subject to the 1987 Maximum of $1,857.95. Thus, increase = $1,857.95 minus 1,500 = $357.95.

4. Step-Down Life Annuities

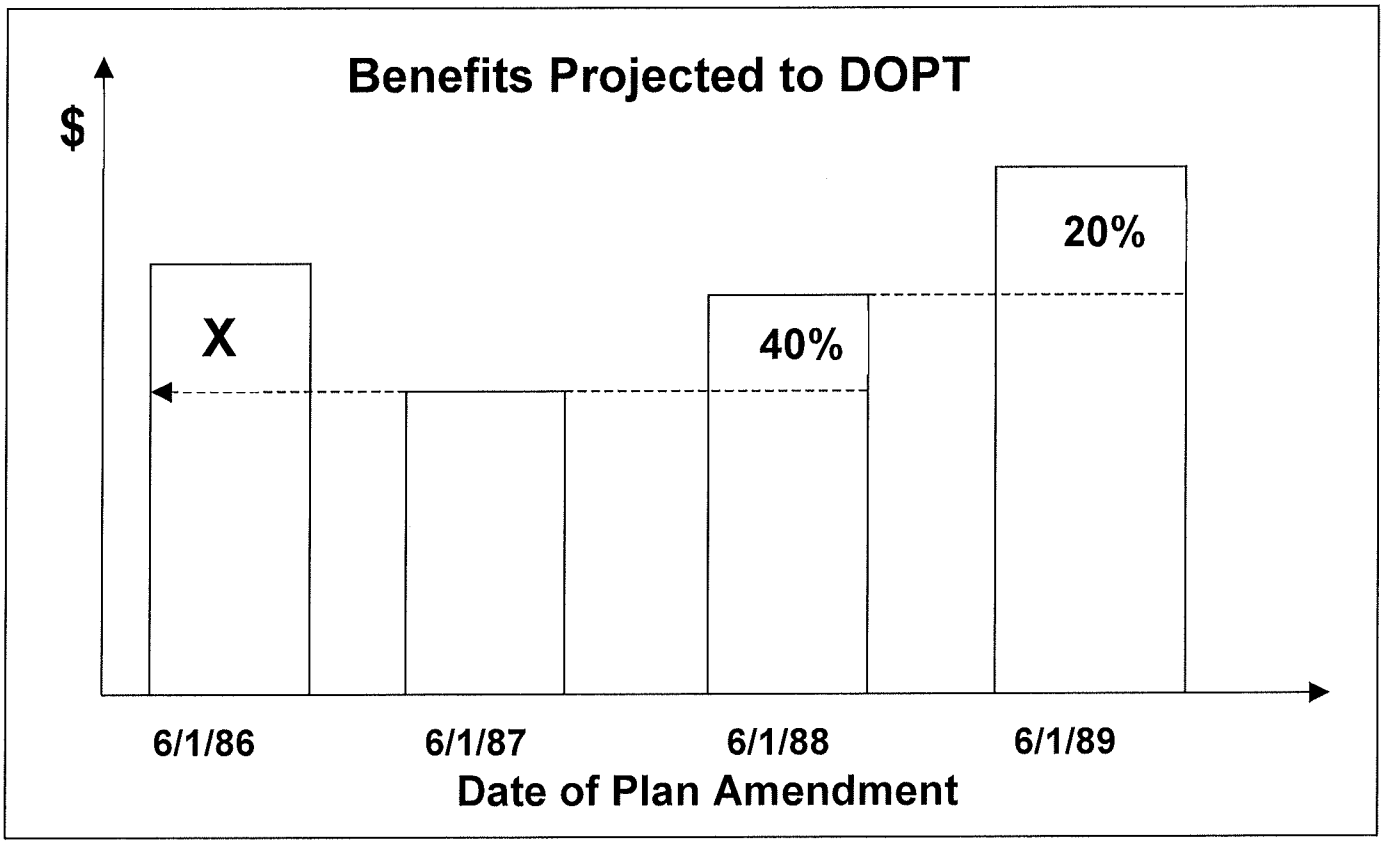
The following procedure is used for determining phase-ins and maximums for step down life annuities.

(1) Limit benefit to the accrued life annuity at normal retirement age.
(2) Determine the amount of the remaining temporary supplemental income benefit exceeding level annuity.
(3) Apply appropriate level life factor from 4022.23(f) to levelize the remaining supplement in (2).
(4) Add levelized supplement in (3) to level annuity (even if a J&S benefit form).
(5) If applicable, lower to maximum (adjusted to final form).
(6) Compute levelized phase-in and add to levelized benefit before amendment.
(7) Convert back to final form by multiplying final step down annuity in (1) by the ratio of levelized phased-in amount in (6) to the levelized final form in (4).

An example of this calculation is given in problem #32 in Appendix A.
If a plan's survivor benefit also decreases at a certain age, then levelize the survivor benefit (the factors can be obtained by calling the PBGC Actuarial Services Division) and redetermine the percent continuation, before proceeding as usual.

5. Benefit Decreases

When there are decreases in projected benefit amounts, phase-in benefit increases only. Assume that the projected benefits that were later eliminated never existed. Consider the example provided below, where the region indicated by an "X" is treated as if it had never existed.



6. Purchased Annuities

For participants in the plan on DOPT with a partially purchased benefit, PBGC will reduce benefits by purchased benefits. If a participant's purchased annuity is greater than the PBGC maximum, the guaranteed benefit can be zero.

7. Benefits that become Nonforfeitable as a Result of a Partial Termination

The additional vesting of a benefit due to a partial termination (see IRC 411(d)(3)) of a plan prior to the date of plan termination is not non-forfeitable for purposes of PBGC guarantees (or for purposes of PC5 - See Chapter VII, Section 5).

8. Plans with Benefit Offsets from Other Plans

If a terminated plan's benefit formula has an offset from another terminated plan, the full offset is used even if the full benefit from that plan is not fully guaranteed.

9.Cost-of-Living Adjustments

COLAs that increased participants' benefits prior to DOPT are subject to the phase-in rules, based on the later of their adoption or effective date of the increase. Thus, a COLA that occurs in the year **prior to** DOPT is 0% phased-in and thus not guaranteed (even if automatic and adopted many years prior to DOPT) due to PBGC's rule to use later of adopted and effective dates. Automatic COLA's occurring after DOPT are not guaranteed.

10. Special Limitation on Aggregate Benefits Payable Out of PBGC Funds

ERISA 4022B places a special limitation on the aggregate guaranteed benefits payable to any individual because of participation (or beneficiary status) in more than one trusteed plan, which terminated without adequate funds to provide all guaranteed benefits. An individual cannot receive more than the maximum guaranteed pension *out of PBGC funds.*

For example, consider a participant age 65 who is eligible to receive a fully phased-in benefit of $1,000 payable at age 65 from his current plan and a $500 single life guaranteed pension at age 65 under a plan that terminated earlier in the year. Further, let us assume that only one-fifth of the $500 pension was funded out of assets from the terminated plan with the balance of $400 funded out of PBGC funds. Under these circumstances, the maximum benefit (Single Life at age 65) which would be payable out of PBGC funds if his current employer's plan terminated would be the current year's maximum minus $400.

11. Section4022(c) Benefits See Chapter VII, Section 8

12. Multi-Employer Guarantees - ERISA Section 4022A

MPPAA benefit guarantees are different than those for Single employer plans. First of all, the plan must be insolvent under 4245(b) or 4281(d)(2) in order to have the PBGC take the plan over and pay the guarantees. Secondly, the PBGC will not pay any of the benefit increases from the last 5 years (using the later of effective and adopted dates). Thirdly, the maximum benefit is a function of the plan's accrual rate. The accrual rate is defined in 4022A(c)(3) as the participant's monthly benefit (excluding increases in the last 5 years) divided by his or her service. This helps smooth out non-level benefit rates and maximum service provisions. The law then guarantees:

100% of the first $11 of the rate, plus 75% of the next $33 times the participant's service.

If the plan has not always been funded appropriately, the 75% changes to 65%. A few examples may be of help here.

Multiemployer Guaranteed Benefit Examples

		Example 1	Example 2	Example 3
1.	Insolvent	Never	Never	Yes
2.	Benefit Formula	$50 x SVC	$16 x SVC	$20 x SVC
3.	Maximum Benefit	N/A	N/A	N/A
4.	Employee's Service	25 yrs	25 yrs	25 yrs
5.	Employee's Benefit	$1,250	$400	$500
6.	Accrual Rate = (5). (4)	1250/25 = 50	400/25 = 16	500/25 = 20
7.	Accrual Rate in excess of $11	$39	$5	$9
Guarantee				
8.	100% of 1st $11 of (6)	11.00	11.00	11.00
9.	75% of next $33	+24.75	+3.75	(65%) 5.85
10.	Guaranteed rate = (8) + (9)	35.75	14.75	16.85
11.	x service	x25	x25	x25
12.	Guaranteed Benefit: (10) x (11)	$893.75	$368.75	$421.25

VI. VALUATION OF BENEFITS

The mortality tables and interest rates used in valuing plan benefits are set forth in the "Valuation of Plan Benefits" regulation 29 CFR 4044. Valuation of plan benefits in M-E plans following Mass Withdrawal are the same and can be found in Part 4281, Subpart B, which references the interest rates and mortality tables in regulation 4044, Subpart B. PBGC valuation assumptions are used for:

1. valuing plan liabilities for Distress and Involuntary Terminations,
2. determining benefits payable under a 4044 asset allocation
3. determining 4044(d) surplus distributions in plans with employee contributions,
4. determining additional vesting when a partial termination occurs - to the extent funded per 411(d)(3),
5. safe harbor calculations for 414(l) spinoffs and mergers of underfunded plans,
6. mergers and spinoffs of insufficient plans,
7. reporting Unfunded Benefi Liabilities to the PBGC for Controlled Groups with Unfunded Vested Benefits > $50 million,
8. deductions under 404(g), and

1. PBGC Trusteed Plans

For pension plans that the PBGC trustees (Distress and Involuntary), the mortality, interest, expense, and retirement age assumptions are as discussed below. The valuation date for these present values is DOPT (Date of Plan Termination) for items (1) and (3) above. The benefit valued is the automatic benefit that would be paid in the absence of an election. Starting in 2002, de minimum lump sums are valued as if they are to be paid in the form of the automatic pension.

a. **Mortality:**

Healthy males - 83 GAM

Healthy females - 83 GAM set back 6 years

Disabled participants not receiving Social Security - the appropriate healthy table as determined above set forward 3 years

Disabled participants receiving Social Security - the PBGC disability table (for people with Social Security benefits) up to age 65, followed by a table parallel to the disability table for participants not receiving Social Security.

b. **Interest:** PBGC interest rates used to value annuities have a select and ultimate structure in that two or three rates will apply to successive periods subsequent to the valuation date, regardless of the actual Benefit Commencement Date. The select and ultimate interest rates can be found in Appendix B to Part 4044 or at PBGC's web page (www.pbgc.gov). An example would be the August 1998 rates of 5.4% for 25 years and 5.25% thereafter. PBGC's interest rates are based on a quarterly double-blind survey of annuity prices (excluding certain loadings) from the American Council of Life Insurers. PBGC determines their interest rates such that combined with the PBGC mortality table they produce the best fit to the ACLI survey prices. Since the survey is only quarterly and is available only with a lag, PBGC uses the changes in a high quality Moodys bond index to determine the monthly change in their initial interest rate during the calendar year.

c. **Expenses:** The expense loading was uncoupled from the interest rates and is determined explicitly as detailed in Appendix C of the regulation. Prior to 1994, the PBGC reduced the interest rate by about 0.5% to reflect expenses. Now the expense loading is a function of the number of plan participants, the liability amount, and the valuation interest rate. It is approximately equal to $8,000 per plan plus $200 per participant plus 1% of plan liability. See Appendix C to Part 4044 for the exact assumptions. The total expense loading for a plan

is allocated to Priority Categories in proportion to the non-lump-sum liabilities in those categories (calculated without expense loading).

d. Retirement Assumption:

The PBGC will pay benefits at Normal Retirement Age, even if the employee is still working at the plan sponsor's business (i.e., they don't suspend benefits after NRD). PBGC can also pay benefits at the plan's early retirement ages, as long as the employee is no longer working at the plan sponsor. Thus, liabilities should reflect early retirement subsidies. In valuation regulation 4044, the PBGC decided to continue to use its simplified approach for valuing early retirement benefits. In lieu of computing the weighted average of the value of the retirement benefit payable at each age early retirement, the PBGC chose to value benefits at a single expected retirement age (XRA). This was adopted to avoid the complexities associated with computing the guaranteed benefit at each age that early retirement is possible. A synopsis of Sections 4044.55 to 4044.57 is as follows:

(1) Closing of a Facility - use earliest retirement age.
- This applies to all actives and separated participants who terminated less than 1 year before DOPT in facilities that were permanently closed down within one year prior to DOPT (or were in the process of shutting down on DOPT).
- If separated more than 1 year before DOPT, use expected retirement ages from Table II-C. The PBGC figures, these participants are more likely to have found a job and thus won't retire as soon as participants who were affected by the shutdown.
- If not a closing, see (2) if active and (3) if separated.

(2) All Active Participants - use Table II-A, II-B, or II-C depending on the size of the participant's monthly benefit at NRA[9], the calendar year the participant reaches NRA[12], and the Table in use on DOPT. The low table (II-A) gives older XRA and is used for participants with small benefits. Table II-C (high) gives earlier XRA and is used for participants with large benefits. Table II-B is the medium table. The theory, of course, is that participants who have larger benefits are more likely to commence benefits sooner.

(3) All Separated Participants - use Table II-C (high) unless the plan requires that separated participants must not be working in the same industry in order to get a retirement benefit. In that case, use Table II-A, II-B, or II-C depending on the benefit amount.

The necessary tables can be found in Appendix D to Part 4044. They have been extended to younger ages by the PBGC. Until they are in the regulation, you can get them from Karen Justensen, Chief Litigation Actuary at the PBGC. It should be noted that these XRA assumptions were developed to value non-forfeitable benefits (whose contingencies have been met), which is appropriate for terminated plans. However, they do not value contingent benefits well since they are not a function of when the contingency is met (and thus may not be very accurate for ongoing plans with early retirement subsidies). They will undervalue both a subsidized benefit for which the contingency is met before or after the expected retirement age assumption. For example, in a plan with unreduced or subsidized benefits upon completing 30 years of service, an employee age 56 with 28 years of service, would most likely retire at age 58. However, the PBGC's XRA may be more or less than 58.

[12] or earliest age for unreduced benefits, if lower.

2. Non-PBGC-Trusteed Plans

a. Annuity Benefits

For sufficient (non-PBGC-trusteed) plans, the "benefit liability" of a participant who will get an annuity is the cost of purchasing the annuity on the distribution date. (Note: The PBGC no longer underwrites the early retirement subsidies.) Participating contracts are allowed if they are an irrevocable commitment backed by the full general fund of the insurance company. If a participating contract is purchased, then a non-par quote will be needed to determine residual assets if some of the residual is payable to the employees. Annuity contracts purchased in settlement of plan liabilities must provide for all of the participant's rights in his or her accrued benefit (see Priority Category 6) including any forms of benefit distribution, any fixed or contingent subsidized optional forms of benefit or early retirement subsidies applicable to the accrued benefit, any rights regarding notice and election periods for a qualified joint and survivor benefit, the QPSA, and obey any limitations on qualified distributions under IRC 415, etc. Benefits must be calculated using plan factors (i.e. not the insurance company's actuarial equivalent factors). Because some insurance companies find it difficult to price contingent unreduced benefits, the IRS suggested in Revenue Ruling 85-6 that plans could be amended to provide the unreduced subsidies to everyone. That could be a nice but expensive solution!

b. Lump Sums

If a participant will receive a lump sum, then that participant's benefit liability equals such lump sum amount, determined as of the distribution date. Plans do not need to offer lump sums. Lump sums can be paid if the employer so desires; however, the plan document needs to permit it. If the lump sum is greater than $5,000 the employee and spouse must consent to its distribution. In addition, the participant must be provided the relative value of the options per Sections 1.417(a)(3)-1 and 1.401(a)-20. The plan can pay a lump sum regardless of the participant's or spouse's wishes if less than $5,000. Even participants in pay status can get lump sums, but both the participant and spouse must consent to it in writing even if $5,000 or less (see §417(e)(1) second sentence).

In 1994, the minimum lump sum calculation produced an amount that was greater than those produced using a 5% interest rate. When applied to large benefits, this could exceed the 415 maximum benefit commuted at 5%. In this situation, the 1994 Enrolled Actuaries Meeting's Gray Book Q&A provided the unofficial IRS answer that the §415 requirement to use 5% to calculate a lump sum overrides the minimum lump sum (determined using the PBGC rate at the time), citing the first sentence of 1.417(e)-1(d)(1).

In RPA94, the rules for determining the minimum lump sum were changed to base them on the 30-year Treasury rate and the 83GAM (1983 Group Annuity Mortality) table. The higher interest rate reduced minimum lump sums, but plans were protected from the anti-cutback rules in §411(d)(6) by GATT section 767(d)(2) per §1.417(e)-1(d)(10)(iii)(A) & (B), unless they had subsidies in their lump sums. The Secretary of Treasury must prescribe a new table once it is in use by a majority of states for group annuity contracts. Per Revenue Ruling 2001-62 the mortality table changed for distributions after 12/31/2002 to the unloaded 1994 GAR mortality table (with 50% male and 50% female) projected to 2002.

The 417(e) minimum lump sum must be stated in the plan document. While PBGC and Treasury rates change monthly, plans are permitted to use one rate for the full plan year - the rate in effect at the beginning of the plan year - 1.417(e)-1(d)(3). Other choices are possible, but the greater of the old and new lump sum methods must be used for a year after a plan adopts a new method - see the transition rule in 1.417(e)-1(d)(3)(iv). What other Treasury rates are allowed? IRS Regulation 1.417(e)-1(d)(4) says the plan must specify:

(a) the stability period - a period of one month, one plan quarter, or one plan year over which the interest rate is used (calendar quarter and calendar year were added by the final reg), and

(b) the lookback month - i.e., the 1st, 2nd, 3rd, 4th, or 5th month prior to the first day of the stability period (the final regulation allows an average of 2 or more consecutive months from above list). The interest rate used is the Treasury from this month. Using an earlier month helps plan administrators with the old 30 to 90 day election period rule. Even with the 7-day rule, it still helps them have time to calculate the lump sum amount.

The same interest rate must be used above and below $5,000 per IRS. Otherwise there would be voluntary lump sums under $5,000 or there would be discrimination problems for voluntary lump sum rates being better. Can a plan eliminate 6% lump sum subsidies if lump sums were only provided when under $5,000? Section 1.411(d)-4, Q&A-2(b)(2)(v) allows plans to cut back or eliminate de minimus lump sum benefits (e.g., the plan can be amended to change its $1,750 threshold for mandatory lump sums, either up or down, and not violate 411(d)(6)). Thus, you might think a plan could eliminate the subsidized de minimis lump sums. The IRS would not say whether this was legal in the 1996 EA gray book.

If the plan provides lump sums, it must provide a lump sum at termination at least as great as the lump sum benefit provided in the plan. IRS regulations 1.411(d)-4, Q&A-2 and 1.417(e)-1(d)(1) state that the lump sum need only be the actuarial equivalent of the employee's nonforfeitable accrued benefit payable at normal retirement age under the plan. In other words, it does not need to include the value of any early retirement supplements or subsidies or J&S subsidies. (Also see the discussion on Tilley v. Mead in Chapter VII, Section 6 on Priority Category 6.) The rationale is that the employee has the option to take the lump sum or not take it. Only the qualified J&S benefit must be as valuable as other options. Sponsors should inform the participant if the lump sum is less valuable. IRS regulation 1.401(a)-20, Q&A-36 says that a written explanation of the relative values of the options (e.g., to the extent to which optional forms are subsidized) must be provided to the employee within a reasonable period before the annuity starting date per 417(a)(3). Note, the 30-day minimum between notice of J&S rights and the benefit payment may be shortened to 7 days if the participant (and spouse, if necessary) consents. Lump sums must include the value of any automatic COLA's per the IRS and PBGC (although not in any regulation). The Ninth Circuit agreed in Shaw v. IAM 750 F.2nd 1458; 6 EBC 1193 that COLAs are a part of the accrued benefit (unless they exceed the 415 maximum benefit without future COLAs). At young ages, 1.417(e)-1(b)(1) warns that the QJSA must also be available for immediate commencement if a lump sum is immediately available.

The lump sum need not include the value of the QPSA, as an IRS spokesperson has stated that the annuity starting date (ASD) of a lump sum is immediate which would mean the present value of the QPSA is zero. Another way to handle this is to amend the plan to charge for QPSA through a reduction in the accrued benefit in the future. Thus the present value of the QPSA is in the present value of the accrued benefit. Plans do not have to use the applicable mortality table in 417(e)(3), but they must be reasonable and the minimum lump sum must use it. Plans should use a unisex table as mandated by the Supreme Court's Norris decision. The conversion basis should be stated in the plan document in order for benefits to be definitely determinable - a qualification requirement for the 1984 plan year by IRS Revenue Ruling 79-90 and now IRC §401(a)(25). In IRC §412(i) fully insured plans, the lump sum can equal the vested

portion of the cash value per IRC §411(b)(1)(F), as long as it is not encumbered by unpaid premiums, loans, or security arrangements.

Applicable Plans: RPA's change to IRC §417(e) and ERISA §205(g) applies to most DB plans. Exceptions include Government plans and certain church plans.

Applicable Benefits: The 30-year Treasury rate and applicable mortality table apply to minimum lump sums and period-certain annuities. They do not apply to non-decreasing annuities payable for at least the lifetime of the participant including a J&S annuity with at least 50% continuation, QPSA, and benefits that may decrease due to supplements, and qualified disability payments. See 1.417(e)-1(d)(6) and Q&A #3 of Rev. Rul. 95-29. The Social Security Leveling Option (SSLO) is probably subject to this rule (since it could calculate out to be a temporary annuity for participants with small benefits). If the SSLO is subsidized, it may not affect the benefit.

Maximum Lump Sum Equivalencies Must Also Use 30-year Treasury:

- Effective Date: GATT and Rev. Rul. 98-1 Q&A #5 mandate that lump sums under 415 must also be calculated using the 30-year Treasury rate. This decreased the maximum lump sum greatly, especially at young ages. Lump sums to young participants in Cash Balance plans were particularly vulnerable to the lower 415 amounts when the 30-year Treasury is high, since these plans are usually much more front-loaded than typical DB plans.
- Reductions for Age: 5% below 62: Before age 62, the maximum § 415 benefit is reduced based on the applicable mortality table and 5% (or plan equivalencies/factors if they cause a greater reduction). Revenue Ruling 95-29 said that 30-year Treasuries replaced this 5%, but the SBJPA reversed the age reductions back to 5%. The 5% has been changed to 5.5% for 2004 and 2005.
- Comparison of Early Retirement Reduction Factors below age 62: Note that under Revenue Ruling 98-1 (Q&A #7- step2 and #9), one does not compare the statutory and plan interest rates, but equivalences using both mortality and interest. This is probably to accommodate tabular ERRFs. In the case of a plan that determines lump sums as the present value of the immediate early retirement benefit, you compare the plan's $ERRF_{ARA}/ERRF_{62}$ with N_{62}/N_{ARA} using 5% and the applicable mortality table. Some plan ERRFs could have a greater reduction than actuarial factors where i=5%. In plans with unreduced benefits at age 62, but with reductions from 65 for age 61 retirements, the $ERRF_{62}$ would be 1.0, which causes a stiff reduction before age 62 to the 415 maximum.
- Forms Other Than Single Life Only: Conversion factors for annuities (except certain period and temporary annuities) must use a conversion factor using 5% and the applicable mortality table (or the plan factor if worse). However, forms subject to 417(e), such as lump sums, must replace 5% with the applicable Treasury rate. The QJSA survivor benefit still does not reduce the maximum 415 dollar limit, per Q&A #7-step 1. Another surprise was provided in Q&A 10 in the 1998 EA meeting Grey Book. If a plan has unreduced early retirement benefits, but the participant chooses a lump sum that equals the present value of the deferred NRB, then the conversion factor is that lump sum divided by the immediate pension, which will cause a harsh reduction to the 415 benefit.
- No Pre-Retirement Mortality? Mortality can still be ignored pre-NRA, to the extent there is no forfeiture at death, per Q&A #6. (Notice 87-21 still applies.)
- Delayed Retirement: Revenue Ruling 98-1 also says that if the plan does not provide actuarial increases post-NRA, then the limit adjustment is not increased actuarially. Q&A #7, Step 2, last paragraph, says use the lower of the plan's actuarial equivalence for late retirement and the ones

using 5% and 83GAM. The dollar limit adjustment can be increased by COLA's for delayed retirement (and after benefit commencement if plan is worded to allow this).

- Applicable Plans: GATT/RPA's 415 change to lump sum rules applies to 417(e) affected plans. The 417(e) change applies to most DB plans. Government plans and certain church plans which are not subject to 417(e) or ERISA §205 only have to use the applicable mortality table, not the 30-year Treasury. Their plans can still use the 5% minimum interest rate. See Q&A #3 of Revenue Ruling 98-1. Fully insured plans (which comply with 411(b)(1)(F) where the accrued benefit equals the cash value) must comply with all of 415, including the applicable mortality table and the 30-year Treasury. See Q&A #23.
- Applicable Benefits: The 30-year Treasuries (not 5%) and 83GAM apply to lump sums and period-certain annuities. However, non-decreasing annuities payable for at least the lifetime of the participant including a J&S annuity with at least 50% continuation, QPSA, and benefits that may decrease due to supplements, and qualified disability payments can still use 5% (not 30-year Treasuries). See Q&A #2 of Rev. Rul. 98-1. The Social Security Leveling Option (SSLO) is probably subject to this rule (since it could calculate out to be a temporary annuity for participants with small benefits). If the SSLO is subsidized, it may not affect the benefit.

VII. ALLOCATION OF ASSETS

Section 4044 of ERISA specifies the procedure for allocating the assets of a terminating pension plan. This procedure can be obtained in detail from the "Allocation of Assets" regulation (29 CFR 4044). Now that standard terminations have to be fully funded through Priority Category 6 (PC6) (effective for plans with Notice of Intent to terminate after 12/17/87), the only times an allocation is performed is for:

(1) Distress and Involuntary Terminations,
(2) Partial Terminations of insufficient plans (to determine who gets vested),
(3) Mergers of insufficient plans (to determine special schedule of higher priority benefits),
(4) Spinoffs and transfers of insufficient plans (to determine the amount of assets to move),
(5) Determining the amount deductible under IRC 404(g) when a plan sponsor promises to make a plan sufficient for a standard termination (unless the deduction under IRC 404(a)(1)(D) is greater),
(6) When PC2 is needed to determine the portion of residual assets, which go to employees.

If a plan were fully-funded upon termination, then participants would receive more than their guaranteed benefits; they would get all the benefits for which the plan is liable. Suppose the plan is almost fully-funded. Each participant would receive at least guaranteed benefits from the PBGC but some would not receive all of their plan benefits. Whose benefits are reduced? The answers to this question are provided by §4044, which establishes priority categories for the allocation of plan assets. (Note: Assets include the collectible value of Due and Unpaid Employer Contributions - DUECs.) Some benefits have more priority than guaranteed benefits. This means that, even if assets do not cover guaranteed benefits, some benefits in excess of guaranteed benefits will be provided for, which results in some plan assets being directed towards employee benefits rather than the PBGC. While the allocation procedure is quite complex, a greatly simplified description of the 6 priority categories follows:

Priority Category 1 - Voluntary Employee Contributions;
Priority Category 2 - Mandatory Employee Contributions;
Priority Category 3 - Retirement Benefits Payable 3 Years Ago (in pay status or could have been);
Calculate benefit at DOPT minus 3 years, using worst plan in last 5 years.
Priority Category 4 - Other Guaranteed Benefits (Substantial Owners get regular guarantee)
Priority Category 5 - Other Vested Benefits; and
Priority Category 6 - All Other Benefits.

Complexities arise in allocating assets because of the interaction between the limitations on guaranteed benefits and the possibility of funding non-guaranteed benefits before all guaranteed benefits have been funded. A brief summary of the characteristics of each priority category is provided below.

1. Priority Category 1

Voluntary employee contributions are not guaranteeable by the PBGC. Hence, the entire value of accumulated employee contributions is non-basic-type benefits. Thus, if the plan had no assets, the participants would not have their voluntary contributions returned. However, it would be quite unlikely that the voluntary contributions account would be empty. The value of priority category 1 (PC1) for each participant is the balance of the separate account maintained for the participant, or the present value of their annuity if already elected in lieu of cash.

2. Priority Category 2

The benefits in priority category 2 (PC2) of each participant consist of the basic and the non-basic type benefits derived from mandatory employee contributions (EEC). Contributions are defined as mandatory if they are required as a condition of employment, participation, or obtaining benefits. If the employer pays the employee contributions, but they are not imputed to be employee taxable income, then they are not mandatory EEC. In general, under the PBGC's current asset allocation regulation, the value of an individual's PC-2 benefit is based on the participant's election:

(a) annuity election - the value assigned as of DOPT to PC-2 is the present value (at PBGC assumptions) of the employee derived annuity plus the present value of the pre-retirement return of contributions death benefit. These are both basic benefits.

(b) refund EEC election - the value assigned as of DOPT is the sum of (a) the basic portion plus (b) a non-basic benefit equal to the excess, if any, of employee contributions with interest to DOPT over (a). Regulation section 4044.12(c)(2)(ii) and (iii) provides that the PC-2 value for those electing a refund may not exceed the value of the employee's contributions with interest.

The next page sets forth a sample PC2 calculation. Consider a 45-year old male participant with an accrued benefit of $100.00 per month payable at age 65 as a single life annuity and Employee Contributions with Interest (EECWI) are $1,000. The plan uses the §411 rate (i.e., 120% of the Federal mid-term rate as in effect for the first month of the plan year) to accumulate employee contributions up to the determination date. After the determination date, one must accumulate EEC using the IRC 417(e)(3) rate up to the Normal Retirement Date and convert to an annuity using those same 417(e) rates. The plan's accrued benefit cannot be less than the monthly benefit that would be purchased by the EECWI.

What is the determination date? The 1.411(c)-1 regulation says it is the date of first distribution and not the date of separation. Thus, the employee's accrued benefit is not fixed at the date of separation, due to the fact that the 411(c) rate changes every year. This can be remedied by paying a lump sum at separation because that fixes the date of determination as the date of separation. For such a plan, the computations are as follows:

Sample PC2 Calculation

PC2 present values can be computed as follows assuming an Expected Retirement Age of 65.[13]

Value of Pension Benefit derived from employee contributions:	
(1) PC2 Monthly Pension	$ 29.80
(2) PBGC Single Premium for Deferred Annuity commencing @ 65	2.2516
(3) Value of PC2 Pension: (1) x (2) x 12	$ 805.27
Value of Death Benefit refunding EEC:	
(4) Accumulated Contributions at 45	$1,000.00
(5) Single Premium for Refund of Contributions accumulated on death[14] = 1.0 - ${}_{20}p_{45}$	.19478
(6) Value of Death Benefit	$ 194.78
Value of Total Priority Category 2 Basic Benefit:	
(7) Total Value: (3) + (6)	$1,000.00

[13] If benefits are commenced prior to NRA, then the benefit must be at least the actuarial equivalent using plan assumptions of (1) the employee-derived accrued benefit plus (2) the vested portion of the employer-derived benefit at NRA. It also cannot be less than EECWI at retirement.

[14] This simple formula for the present value of the return of employee contributions upon death presumes that they are being valued at the accumulation rate. A problem arises if the plan accumulates the EEC at something else.

Non-Basic

The non-basic-type benefit is set equal to zero, if the participant chooses an annuity. If the employee elects to withdraw his/her EECWI, then the present value of Category 2 equals the amount of the EECWI.

Allocation

If the Plan is not funded through Priority Category 2, and an election of the return of mandatory employee contributions is made consistent with plan provisions, the PBGC will pay in a single installment, at least the present value of the basic-type benefits provided by mandatory employee contributions - 4022.7(b)(2). Note that the present value of the full basic-type benefit is returned, and not just the guaranteed portion. This rule primarily comes into play when the phase-in cuts back the guaranteed benefit to less than the employee-provided benefit.

If the plan assets exceed the value of the basic-type benefits provided by the mandatory employee contributions, then the PBGC will pay, upon election, the funded amount of PC2. In all cases, if an employee elects withdrawal of EECs, then the Title IV benefit is reduced by the full employee provided benefit, even if full employee contributions were not returned.

3. Priority Category 3

Priority Category 3 (PC3) includes any benefit payable as an annuity based on the provisions of the plan in the last 5 years under which the benefit would be the least for participants or beneficiaries who were in pay status on DOPT-3 (or would have been if they had retired and commenced benefits on that date under the normal form). Note: DOPT-3 is shorthand for DOPT minus 3 years. The PC-3 benefit is not limited by the PBGC maximum guarantee or by the PBGC phase-in. Thus, it can give certain older participants more than PBGC guarantees. In addition, supplements can be paid in PC-3 even though not guaranteed.

All the following rules from the regulations are based on interpreting 4044(a)(3). Thus,

a. Plan amendments increasing benefits must have been effective and adopted at least 5 years before DOPT in order to affect PC3 benefits. A plan must have been adopted and effective for 5 years in order for any benefit to be in PC3.

b. Scheduled increases in benefits effective between DOPT-5 and DOPT-3 are included in PC3 benefits if adopted and effective on or before DOPT-5. This provision enables the PBGC to guarantee scheduled COLA's up to DOPT-3. (Note: Congress surely did not intend for the benefit increase in PC3 for eligible actives to be greater than the increase in PC3 for retirees and the PBGC regulation states that explicitly.)

c. The PC3 benefit is the one accrued as of and commencing on DOPT-3. It is the benefit in pay-status for those retired before DOPT-3 (excluding schedule increases described in b).

d. The present value factor is still based on the age at DOPT and the benefit form remaining at DOPT for those retired on DOPT. For those not retired at DOPT, benefits are assumed to begin at expected retirement age. (See h.)

e. If the plan on DOPT-3 would have allowed benefit commencement then, but the DOPT-5 plan would not have allowed immediate commencement at DOPT-3, extend the DOPT-5 plan's early retirement factors by the PBGC actuarial equivalent factors for earlier commencement. See Question 19 in Appendix A.

f. The surviving spouse of a participant who was retired on DOPT-3 (or eligible to retire on DOPT-3) is eligible for a PC3 benefit. The benefit is determined by assuming the participant had died at DOPT-3.

g. If a participant's PC3 benefit is greater than their guaranteed benefit, then it makes sense for such participant to retire immediately. The PBGC follows this rule just like when determining the Expected Retirement Age for someone with unreduced benefits.

Three examples of PC3 benefit calculation may be helpful.

DOPT = 1/1/90
Benefit = $10 x SVC on DOPT-5. The benefit was amended up $1 each year.
Early Retirement @ 55 and 10
Normal Retirement @ 65
ERF = 5% per year early
Assume benefits are payable for life.

Participant #1 retired on DOPT-4 at age 61 with 10 years of service (yos)

Benefit @ 61 = $11 x 10 yos x (1 - 4 x 5%) = $88
PC3 Benefit = $10 x 10 yos x (1 - 4 x 5%) = $80
PC3 Liability= $80 x $\ddot{a}_{65}$ (as he is now age 65 on DOPT)

Participant #2 active on DOPT, age 60, with 12 years of service. Not in PC3, because not eligible for a benefit at DOPT-3.

Participant #3 active on DOPT, age 60, with 15 years of service. On DOPT-3, the participant would have been age 57 with 12 yos.

PC3 Benefit @ DOPT-3 = $10 x (15-3) yos x (1 - 8 x 5%) = $72.

The $10 benefit was used because PC3 must use the rate in the DOPT-5 plan.

PC3 Liability = $72 x $_{XRA-60|}\ddot{a}_{60}$

Allocation

An allocation in PC3 needs to be made when benefits in PC3 are not guaranteed (i.e. some PC3 benefits can be non-basic). Examples are:

(1) benefit amounts in excess of the maximum insurance amount,
(2) benefits in excess of the substantial owner guarantees,
(3) benefits created by scheduled increases between DOPT-5 and DOPT-3 and not phased-in, and
(4) benefits in excess of the accrued single life benefit payable at normal retirement.

Note, however, that a PC3 allocation cannot help someone whose benefit was only cut by a phase-in (except the rare situation in item (3) above) because the PC3 benefit is from the plan with the least benefits over the last 5 years. In fact, one would not have to calculate PC3 benefits for the above 3 examples because the phased-in benefit would have been greater.

If assets remain after allocation to all of PC1 and PC2, they are allocated to the total PC3 (basic and non-basic). If they do not cover total PC3, then the percentage covered is determined. This percentage is then multiplied by each participant's total PC3 liability. The resulting assets are first applied to the participant's basic-type benefits and then to their non-basic-type benefits.

An allocation in PC3 does not need to be performed if (1) the assets are so small that they cannot help any participant (check those with the largest cutbacks) or (2) the assets exceed the present value of vested benefits (i.e. assets cover PC5).

4. Priority Category 4

This category includes all guaranteed benefits not assigned to priority categories 2 and 3 as well as those non-guaranteed benefits which would be guaranteed in the absence of the special limitation on guaranteed benefits for substantial owners or the aggregate payments limitation. Thus, Substantial Owners can get more than their S/O guaranteed benefit if there are enough assets in PC4. This could happen if assets allocated to the regular guaranteed benefits are enough to exceed the S/O guarantee. The following 2 examples may help.

Substantial Owner PC4 Calculation
(Benefits are annual amounts.)

1.	Plan Assets available for PC4 (given)	$ 50,000	$ 20,000
2.	Present Value of total PC4 benefits for all participants (given)	200,000	200,000
3.	Ratio of (1) to (2)	25%	10%
4.	S/O's total PC4 Benefit in Item 2 (given)	3,000	3,000
5.	S/O's Benefit from allocation: (3) x (4)	750	300
6.	S/O's guaranteed benefit (given)	600	600
7.	S/O's PC4 benefit-greater of (5) & (6)	750	600

The value of priority category 4 benefits is the value of the PC4 benefit at the expected retirement age (or DOPT if in pay status) less the value of the PC2 and PC3 benefits (payable beginning at XRA, or DOPT if in pay status).

5. Priority Category 5

PC5 contains all remaining nonforfeitable benefits under the Plan. Benefits that become nonforfeitable as a result of termination or prior partial termination (see IRS Reg. 1.401-6) of a plan will be considered forfeitable for PC5 purposes.

The definition of nonforfeitable in ERISA 4001(a)(8) should be reviewed to help in understanding what benefits are in PC5. The following examples may be of help.

a. The **subsidy in optional forms** not automatic (or elected) on DOPT are considered to be in PC5, if the underlying benefit is vested and the employee is eligible to receive it. These subsidies are not in the allocation earlier because they are not a basic-type benefit, due to the entitlement requirement of section 4022.4.
b. The **subsidies in early retirement benefits** are not in PC5 if the employee has not satisfied the age and/or service requirements on DOPT - i.e. not nonforfeitable per ERISA 4001(a)(8).
c. Benefits **contingent** on future events such as disability, death or contingent on future employment are not non-forfeitable on DOPT and thus are not in PC5.
d. However, due to ERISA 4022(e) making the qualified pre-retirement survivor annuity **(QPSA)** nonforfeitable, the QPSA must be offered in PC5. An actuarially equivalent reduction in accrued benefits can be charged to pay for the QPSA. It is not included earlier in the allocation process because it is an ancillary benefit - not a pension benefit. Thus it is a non-basic-type benefit, and the PBGC does not guarantee it. However, the PBGC has decided to offer administratively its own pre-retirement survivor annuity coverage for REA plans not funded through PC5. For participants who elect this coverage, there is a reduction in the benefit amount. Note: If the QPSA is not an accrued benefit, then a plan can be amended to charge for the QPSA, without violating the provisions against decreasing accrued benefits in IRC 411(d)(6) - See Q&A 21 of the Final REA regulation 1.401(a)-20. Q&A 13 of IRS Blue Book provided at the 1990 EA meeting said that QPSA was not 411(d)(6) protected, so a plan with free QPSA can be changed to start charging for it.
e. **Supplemental benefits** (defined in 411(a)(9) of the Code and 1.411(a)-7(c)(4)) are in PC5. However, note that they are not protected by IRC 411(d)(6) because they are not retirement benefits (because they are not paid throughout retirement) and thus can be removed from a plan, which of course removes them from PC5. (Be careful however as participants may contend they have a contractual right to them). The same is true for **shutdown benefits** (supplements payable to age 60, 62, or 65 or payable for life) if the shutdown has not occurred as of plan termination per GCM 39869. The GCM suggests that even the shutdown supplements that are payable for life do not BECOME accrued benefits until the shutdown event. Thus they can be amended out of the plan without worrying about violating the anti-cutback provisions in 411(d)(6). Also see *Richardson v. Pension Plan of Bethlehem Steel Corp. and Subsidiary Cos.*, CA9, No. 93-36089, 5/2/97, where Bethlehem Steel was able to avoid paying it's shutdown benefits. This may have changed.
f. **Automatic COLA's** that are scheduled post-DOPT are in PC5 for vested participants (and in PC6 for non-vested participants). Although they are protected by 411(d)(6) per the Ninth Circuit decision in 1985 in Shaw v. IAM Pension Plan, 6EBC1193, future COLA's are not guaranteed (in PC4) because future COLA's are not subject to phase in.

Allocation

Assets are allocated in PC5 first to the value of benefits in the plan on DOPT-5 but not covered by earlier priority categories. If assets cover that plan, then assets progress amendment by amendment up to the most recent. The amendment upon which assets are used up is allocated pro rata.

If a plan is less than 10 years old, or if benefits have been materially increased within the past 10 years, benefits in excess of guaranteed (or in excess of the maximum guarantee for non-substantial owners)

provided by an allocation to non-guaranteed benefits in PC4, PC5 and PC6 to certain highly paid participants (top 25 on effective dates) used to be reduced to satisfy Treasury Reg. 1.401-4(c). In 1984, IRS Regulation 1.401-4(c)(7)(iii) extended this reduction into PC3. Revenue Ruling 80-229 provided that this limitation does not apply if assets are sufficient through PC6. This is superseded by the more liberal final Regulation Section 1.401(a)(4) - 5(b) which refers to HCEs. The final regulation only allows payment of a straight life annuity equivalent to the accrued benefit plus the supplement to HCEs unless the plan is funded over 110% of CL after paying the HCEs their benefit or if the value of the HCE employee's benefit is less than 1% of CL or less than $5,000. The restrictions can be limited to just the highest paid 25 HCEs.

6. Priority Category 6

PC6 covers "all other benefits under the plan". See 4044(a)(6). PC6 clearly covers all remaining accrued benefits that are protected by 411(d)(6). Even though not accrued, lifetime early retirement benefits (including the subsidy) and optional forms are treated as accrued by 411(d)(6) and cannot be cut. This means they are in PC6 also, since they must be paid before a reversion is taken under 401(a)(2).

a. Non-vested accruals

PC6 includes non-vested benefits that vest to the extent funded upon plan termination per 411(d)(3). In a distress termination it is possible that all of PC6 will not be funded. In standard terminations PC6 has to be fully funded.

b. COLA's are in the accrued benefit per IRS and PBGC. The Ninth Circuit agreed in 1985 in Shaw v. IAM Pension Plan, 6EBC 1193.

c. Contingent Benefits protected by 411(d)(6)

PC6 also includes the contingent subsidy in unreduced benefits (at, for example, 55 & 30) if the participant satisfies the eligibility requirements with post-DOPT service per IRC 411(d)(6) and Rev Rul 85-6. Service with a successor employer could be counted under the "same desk rule" if the employee-participant is basically working at the same place (or same bus, etc.) and if the successor employer bought out the prior employer, assets and liabilities, through say a sale of stock, and took over the plan, per Rev. Rul. 86-48 and GCM 39824. Alternatively, the successor employer could have only purchased the assets (e.g. office, plant, buses, planes, etc.) of the prior company and did not take over the liabilities of the company or the pension plan. In that case, service does not continue, even though the employee is working at the same desk (or same bus, etc.). The plan document could also have required the age conditions to be met upon separation for early retirement subsidies. In that case, an asset sale before meeting the age condition hurts the employee. Liability sales can hurt or help a participant. Continuing in service can help an employee get a subsidized benefit. (This was the situation in Edwin Kotrosits et al v. GAT Corp; US District Court for Eastern District of Pa, No. 88 - 1835 (757 F Supp 1434), where the Judge ruled for employees after a stock sale.) On the other hand, after an asset sale, an employee could reach Normal Retirement and commence a benefit while still working at the successor employer, whereas under the stock sale, an employee's benefit commencement could be deferred until (s)he stops working at the successor employer. Therefore, no matter which way the decision is made, employees might sue.

Another case has added a twist on asset sales. In September 1993, the Third Circuit upheld the same desk rule for workers at PVC Division expecting contingent early retirement benefits and found that the prior employer (Hoechst Celanese) should have transferred additional plan funds for those benefits. The courts decision may have relied on the fact that plan assets were transferred to the new plan under ERISA §208 (Code 414(l)) and thus plan liabilities were transferred - and service too - and that no separation from service occurred. Hoechst argued unsuccessfully that this would remove its incentives to negotiate with the purchaser for continued employment of its former workers. The Supreme Court refused to intervene (Hoechst Celanese Corp. v. Gillis, U.S. Supreme Court, No .93-1284, 4/18/94). In another Third Circuit case (Dade v. North American Philips Corp., CA3, No. 94-5546, 11/1/95), Philips sold Magnavox, but retained the plan assets and liabilities. They vested everyone and gave service towards the "rule of 85" requirement to all their former employees who went to work for the buyer for up to a year, but no more. Employees sued to have all service with the buyer so applied, but the District Circuit dismissed the suit and the Third Circuit affirmed. The DC Circuit also agreed in a similar case [(Andes v. Ford Motor Co., 1995 US App. LEXIS 34438 (D.C. Cir. 1995)] where employees claimed the employer violated ERISA's §204(g) anti-cutback rule

and ERISA §510 (can't interfere with vesting, etc.). In December 1993, the Eighth Circuit in Hunger v. AB, 1993 WL518588 (8th Cir. 1993) stated employees could not use service with the purchaser to help them obtain benefits. In Hunger, the seller, Clevite, sold the assets of its Engine Parts Division to JPI Merger, Inc., but no plan assets were transferred to the new plan.

There is some confusion as to what contingent benefits are in PC6. In a termination prior to REA's protecting these contingent early retirement benefits, the Fourth Circuit Court held in Tilley, et al. v. The Mead Corporation, 815 Fed. 2d 989 (4th Cir. 1987), that five employees who had satisfied the service requirement but not the age requirement for unreduced benefits at 62 and 30, "were entitled to have early retirement benefits considered in determining the amount of their lump sum retirement payout", with the reductions from age 62, not 65 (paragraph 8905). The employees had contended that the sale of their subsidiary and termination of their plan kept them from later qualifying for the unreduced early retirement benefits. This case was appealed and the Supreme Court reversed the 1987 decision, saying that PBGC's Priority Category 6 does not create benefit entitlements (it only prioritizes them), and sent the case back to the lower court with instructions that IRS and PBGC rules be given credence. Mead Corporation v. Tilley, U.S., 109 S. Ct. 2156 [10 EBC 2519] (1989). In February 1991, the U.S. Court of Appeals for the 4th Circuit held in Tilley v. Mead Corp., CA4, No. 86-3858, Feb. 26, 1991, that under the terms of Mead's plan, no reversion was available unless all contingent rights were satisfied and the surplus was due to actuarial error. Contrary to using the IRS definitions of these terms (see section 9 of this chapter and 1.401-2) the court used definitions which helped them find for the employees. PBGC filed an amicus brief requesting this case be retried en banc (i.e. before all judges on the 4th Circuits of Appeals). In another related case, the Third Circuit, noting the Supreme Court's rejection and remand of Tilley v. Mead, held that contingent early retirement subsidies did not need to be honored before a reversion could be paid - Nobers v. Crucible Inc., 13E.B.C.2741 (3rd Cir. 1991) (filed Jan. 29, 1991). The IRS and PBGC contend that these contingent rights do not need to be paid if employees do not work until the age requirement is met. See 411(d)(6) added by REA. Since this is a pre-REA case, the PBGC and IRS contention was even stronger for back then.

Some pension practitioners believe that the subsidy in a lump sum option can be reduced by plan amendment, because it is not a retirement-type subsidy and thus not subject to the anti-cutback rule on accrued benefits found in 411(d)(6), as amended by the Retirement Equity Act. They say Section 411(d)(6)(B)(ii) only says that the lump sum option cannot be eliminated. (It can be eliminated for future service.) It must be at least the actuarial equivalent using 417(e) assumptions. The Tenth Circuit in Steiner Corp. Retirement Plan v. Johnson and Higgins of California, CA10, No. 92-4106, 7/8/94 might agree with them. In this court case the 10th Circuit agreed the actuarial consulting firm was negligent in not timely suggesting that the plan reduce/eliminate its lump sum subsidy when it first had to specify factors in the plan document in 1985. The present value calculation must be specified in the plan per Revenue Ruling 79-90 and IRC 401(a)(25) and must be preserved on the accrued benefit as of the amendment date. Temporary and Proposed IRS Regulation 1.417(e)-1T(d)(10) says that reducing the lump sum calculation method is generally not allowed by 411(d)(6). There are some exceptions due to RPA94 that are discussed in Chapter VI.

d. Contingent benefits not protected by 411(d)(6) and QPSA's

Benefits contingent on future events such as disability and death are not accrued on DOPT. Some pension practitioners believe, that termination of a plan automatically amends these benefits out of PC6. Others would rather be safe and thus they amend the plan to delete future disability, death, and supplemental benefits from the plan on DOPT. Once deleted, they do not need to be included in benefit liabilities. Note: The **QPSA** cannot be removed from the plan, but ERISA does allow an actuarial charge for it. The Q&A 13 of IRS Blue Book provided at 1990 EA meeting said QPSA was not protected under 411(d)(6), so a plan with free QPSA can be changed to start charging for it. *If the plan does not make such an amendment, then its Benefit Liabilities include the cost of the QPSA.*

The committee report to REA said that death, disability, medical benefits, Social Security Supplements, or temporary shutdown supplements that do not continue past NRA are not retirement-type subsidies protected by 411(d)(6). Thus, these benefits can be removed from a plan (and not violate 411(d)(6)). Even the ones in pay status can be removed (although you would run into severe PR and contractual problems if you did this. (See Wean in Chapter III, Section 2(a)(11)). Since the Committee Report did not list in its exceptions "subsidized early benefits payable upon future shutdowns" it was unclear whether they were protected. One needs not only service to obtain this benefit; one also needs a future event such as a shutdown to get the benefit. In this respect it may be like a death benefit. GCM 39869 published on April 20, 1992 clarified this by stating that "shutdown benefits that are retirement-type benefits, and not ancillary benefits, become accrued benefits and, therefore, are protected benefits under 411(d)(6) upon the occurrence of the event that triggers the right to payment of benefits (i.e., the contingent event)." So maybe lifetime supplements and subsidized early retirement factors triggered by shutdowns can be cut before the shutdown event, just not after. See more on this in the PC5 section on supplements and shutdown benefits.

e. Future accruals

Another court case, Blessit v. Retirement Plan for Employees of Dixie Engine, 817 Fed.2d 1528 (11th Cir. 1987), highlights some confusion over what "all other benefits" includes in PC6. This confusion stems from the fact that the final language of ERISA does not have the word "accrued" in PC-6. The Eleventh Circuit Court of Appeals (Florida, Georgia, and Alabama) held in Blessit that before the reversion of assets can occur, "all other benefits" included benefits based on service projected to retirement. The PBGC asked for a rehearing before the full court, and the full court (i.e., the court sitting en banc) vacated its earlier decision. Blessit was appealed to the Supreme Court by the employees, but was not granted a hearing (i.e. no writ of certiorari).

f. Separated non-vested and partially vested employees

The IRS District offices have been known to require that non-vested and partially vested participants who separated within 1 year of DOPT (or who have not incurred a 1 year break-in-service) must become fully vested in PC6 before assets can revert. IRS authority here is 401(a)(2), which says a plan cannot revert assets until all benefit liabilities have been satisfied. (Some districts even use a 5-year look back on post-REA terminations). The IRS National Office has not stated its opinion yet. The confusion arises due to whether an IRS General Counsel Memo (GCM 39310 issued 4/4/84) for a defined contribution plan also applies to defined benefit plans. The GCM says that a partially vested, separated participant from a DC plan who had not had a break in service must vest in his full accrued benefit to the extent funded.

The case of Bouchard v. Crystal Coin Shop, Inc., C.A. No. 85-3942-C (D.C. Mass. April 28, 1987), also focuses on the question of whether a separated participant has already forfeited his non-vested benefits at the time the plan terminated. In this case, the plan did not have the mandatory cash out provision. The court held that without those words, the participant had to consent to a cashout, even if $0. Since the participant did not consent, the court held that there was no forfeiture and that the employee (Bouchard) should get his $17,144. In another case, Borda v. Hardy, Lewis, Pollard, and Page, P.C. et al. (6th Cir. 1998) No. 97-1004 the court held that the employee was entitled to only the vested portion. The court held he was not Aaffected@ by the termination of the plan, only by termination of the employer, if that were to happen. The IRS National Office is currently considering how this issue applies to DB plans. An IRS actuary has said that there could be a liability for non-vested separated employees in current liability, based on their accrued benefit and a probability that they could resume covered employment. Whatever IRS decides, they have said it should not be applied retroactively.

The additional vesting can be avoided on separated participants who received lump sums or irrevocable commitments from insurance companies. IRC 411(a)(7)(B) allows this as it says such employee's service can be disregarded after the cashout unless "returned" upon re-employment per 411(a)(7)(C). There is a question as to when a separated participant forfeits his contingent non-vested portion, or what exempts non-vested and partially vested participants who have not been cashed out from becoming fully vested. Some plans use sections 411(a)(4)(D) and (6)(B) to contend that the separated participants have to return before reclaiming their pre-break service. Participants will contend that these sections apply only for purposes of determining a participant's vesting percentage while service or accrued benefits are not forfeited. Section 411(d)(3) does not really say much more than the following. The rights of all affected parties (separated employees would be affected as they could not re-participate[15]) to their accrued benefits are nonforfeitable upon termination (to the extent funded). However, if they have not reclaimed their service through re-participation, maybe they do not have an accrued benefit either. For non-vesteds who have a break of more than 5 years (or the years worked if greater), the answer may be easier. Section 411(a)(6)(D) lets the plan permanently ignore such prior service (i.e. even if they do return) for vesting purposes.

Consider a partially vested participant who was already in pay status or lumped out. Is a terminating plan now responsible for vesting this individual 100% in his/her accrued benefits? Section 411(a)(7)(B) only says no if the participant received the lump sum. Increasing a retiree's benefit, just because (s)he was only partially vested before DOPT, could be a strange result. If an annuity was purchased for the employee, it might have to be distributed (i.e. the employer is no longer the contract holder or liable for benefits), then the participant might not get any further vesting. One solution: the plan could state that non-vested separated employees are considered cashed out at separation and all benefits are considered forfeited.

The PBGC includes a liability for the non-vested portion for employees who have not had a one-year break. If there is a mandatory cashout provision in the plan, then PBGC deems a cashout of $0 has been made, and therefore, there are no additional benefit liabilities for the non-vested separated participant (or nonvested portion of a separated partially vested who was cashed out).

[15] In Flanagan v. Inland Empire Electrical Workers Pension Plan & Trust, CA9, No. 91-36188, 8/30/93) the 9th Circuit said that under the rule of parity separated employees with 4 years of service, were "affected participants" under 411(d)(3) when the plan terminated within 4 years of their separation, and thus they retained their accrued benefits.

7. Illustration of Asset Allocation

To illustrate the allocation procedure, a hypothetical termination will be assumed. In the illustration below, it will be assumed that neither participant is a substantial owner or has received an unfunded guaranteed benefit under some other terminated plan. Gross benefits and present values in the 6 priority categories follow below. There are 2 lines for PC5; one is prior to an amendment and the other is post-amendment.

Priority	Participant #1		Participant #2		Total Cumulative	Net Value in
Category	Benefit	PV	Benefit	PV	PV	Category
1	-	-	-	-	-	0
2	-	-	-	-	-	0
3	$3,000	$300,000	$ 600	$30,000	$330,000	330,000
4	1,500	150,000	1,000	50,000	350,000	20,000
5a	4,000	400,000	800	40,000	450,000	100,000
5b	5,000	500,000	1,300	65,000	565,000	115,000
6	5,000	500,000	1,300	65,000	565,000	0

If the plan had $220,000 in assets including collectible DUEC's, then they would cover 67% of PC3. In this case Participant #1's funded PC3 benefit would be 67% of $3,000 or $2,000. As this funded portion is more than their guaranteed benefit (PC4), they would receive the $2,000 per month from the PBGC. On the other hand, Participant #2 would receive the $1,000 per month guaranteed benefit (value = $50,000) - because it is greater than the funded portion of their PC3 benefit (67% of $600 = $400). Thus, the total present value of benefits paid by the PBGC will be 67% of $300,000 for Participant #1 plus $50,000 for Participant #2 for a total of $250,000 (which is more than the plan's assets). This example shows how a plan's assets can exceed the present value of guaranteed benefits and yet the plan would still have unfunded guaranteed benefits. I.E. Plan assets have been directed from paying guaranteed benefits to paying for large PC3 benefits. In order for the plan to be sufficient through PC4 the assets would have to equal $350,000 as demonstrated below.

	Present Values		
	Participant #1	Participant #2	Total
PC3	$300,000	$ 30,000	$330,000
Net PC4	0	$ 20,000	20,000
Total PC3 & 4	$300,000	$ 50,000	$350,000

If assets equaled $500,000, the allocation would proceed as follows:

Total Plan Assets	$500,000
Net Value of PC3	-330,000
Remaining Assets	170,000
Net Value of PC4	- 20,000
Remaining Assets	150,000
Net Value of PC5a	-100,000
Remaining Assets	50,000

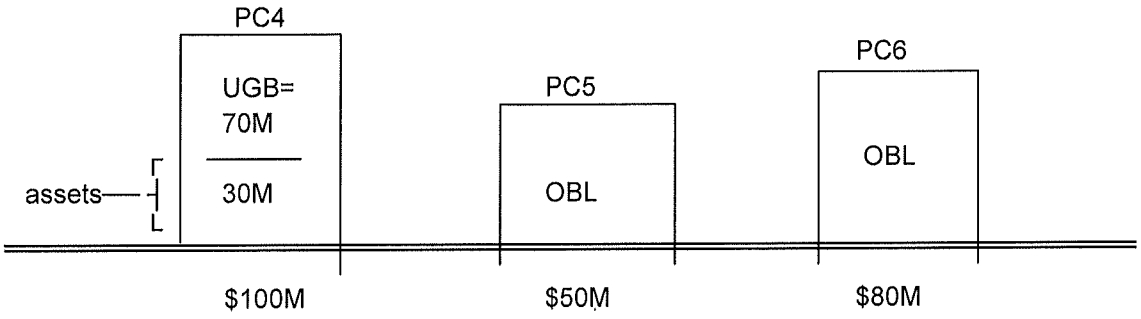
Since $50,000 of assets remain after priority category 5a and the value of priority category 5b is $115,000, the remaining assets will have to be pro-rated among participants in proportion to the value of their priority category 5b benefits. Thus each participant will receive 100% of their priority category 3 through 5a benefits and 43.48% (50,000 divided by 115,000) of their priority category 5b benefits. Participant #1 will receive $4,435 per month (4000 + .4348 x 1000) and participant #2 will receive $1,130 (1000 + .4348 x 300) per month. In this case, there would be no employer liability to the PBGC since all guaranteed benefits were funded. In post-SEPPA plans, there will be an employer liability owed to the participants. In post-PPA plans, the PBGC collects that liability as discussed in the next section.

8. §4022(c) Benefits

As will be seen later, the employer is liable to the PBGC for not only the unfunded guaranteed benefits paid by the PBGC, but also for the outstanding benefit liabilities (benefit liabilities in excess of what the PBGC would otherwise pay due to guarantees and the 4044 asset allocation). Amounts that the PBGC expects to collect from employers is shared proportionately with the employee's portion of the claims (i.e. their outstanding benefit liabilities or OBL's). For small plans (i.e. plans with outstanding benefit liabilities - or OBL's - under $20 million), the PBGC determines an average recovery ratio (collection on all plans divided by the sum of their UBL's). For large plans (OBLs over $20 million), the recovery ratio equals the *actual* collections of that plan divided by their total UBL. The recovery ratio is then multiplied by the employees' outstanding benefit liabilities and this amount of money is allocated to participants through a second allocation process. This second allocation process is more complex than the one described earlier. The first step is to determine the benefits of each priority category. Then reduce them by the funded or guaranteed benefits that will be paid by the PBGC (i.e. Title IV benefits). The net outstanding benefit liabilities in each priority category are then funded by the participants' portion of the collections. The second allocation provides additional benefits beyond those provided by PBGC guarantees and a 4044 allocation from collections on employer liabilities. Consider the following helpful definitions in the forthcoming analysis-

1) unfunded benefit liabilities (UBL) = amount of benefit liabilities minus assets of the plan
2) outstanding benefit liabilities (OBL) = amount of benefits liabilities minus for all participants the greater of their guaranteed benefits or allocated benefits to which assets of the plan are allocated under 4044
3) recovery ratio (RR)=ratio of
   a) amounts collected on employer liability, to
   b) the plan's unfunded benefit liabilities under the plan.

Consider the chart that follows. Here it is assumed that the plan has no mandatory employee contributions and that no one is eligible for a benefit at DOPT-3. And finally it will be assumed there are no benefits in PC4 that are not guaranteed and that $20M is received on employee liability claims. Thus, the recovery ratio equals 10% =20M. (70M + 50M + 80M).



The PBGC allocates an additional amount determined by multiplying the recovery ratio (10%) and the outstanding benefits liabilities ($130M). Thus, $13M will be paid to the participants in PC5. This 4022(c) allocation of the $13M skips over PBGC's loss and all of it ends up in PC5. None makes it into PC6 even though they were a large portion of the claim ($80M). PBGC receives 10% of its $70M portion of the claim directly (i.e., $7M). In effect, it is allocated in PC4 to the PBGC.

	The RR X OBL	= 10% x $130M	= $13M which is now allocated to PC5.
+	The RR X UGB	= 10% x $ 70M	= $ 7M which goes to PBGC
	The RR X UBL	= 10% x $200M	= $20M is amount collected

If OBL, $20,000,000 the PBGC determines an average recovery ratio for all such small plans, as described earlier.

9. Residual Assets and All Benefit Liabilities

Once all benefit liabilities are satisfied by annuities, or lump sums (see Chapter VI, Section 2), any residual assets may be distributed to the employer if the plan specifically provides for such reversion (and it does not contravene any provision of law - ERISA 4044(d)(1)). Unions will argue that in union negotiated plans, the employers cannot take the reversion, since the contributions were really deferred wages, and bargaining agreements directed them to the pension plan. "All benefit liabilities" are defined in ERISA 4001(a)(16). The legislative history of PPA's bill, increasing the plan's termination liabilities from benefit commitments (generally vested benefits - see PC5) to all benefit liabilities (generally through PC6), defines them by reference to IRC 401(a)(2) (see IRS regulations 1.401-2 and 1.401-6) and says the term "includes all fixed and contingent liabilities to plan participants and beneficiaries, including liability for benefits in effect on the date of termination that are not protected under" the anti-cutback rules of "Section 411(d)(6) of the Code or Section 204(g) of ERISA." Pre-ERISA Treasury regulation 1.401-2(b) states that 401(a)(2) "permits an employer to reserve the right to recover at the termination of the trust, and only at such termination, any balance remaining in the trust which is due to erroneous actuarial computations during the previous life of the trust...if, however, the surplus...had been accumulated as a result of a change in the benefit provisions or in the eligibility requirements of the plan, the [surplus] could not revert to the employer because such surplus would not be the result of an erroneous actuarial computation." (Emphasis added) The litigation in Tilley v. Mead was over the definition of "erroneous actuarial computation". See the PC6 section of this chapter. To be safe, many practitioners amend out certain unprotected benefits, such as future death and disability benefits, from the plan on or before DOPT. Insurance companies find it difficult to administer and price these benefits.

Who Gets Surplus? In the past, sponsors could amend their "silent" plans right before DOPT to say that the residual assets revert to the employer. Now, an amendment which increases the reversion will not go into effect for 5 years (e.g. an amendment that expressly increases the reversion to the employer such as going from 50% to 100% of the residual) per ERISA 4044(d)(2). However, an amendment increasing the reversion through elimination of a non-protected benefit (such as future death and disability benefits) could be allowed to take effect immediately (see instruction # 17 to PBGC Form 500 prior to 1993). Plans have done this successfully for years without IRS objections. IRS declined to answer this question in the 1995 EA Grey Book (Q&A #49), saying PBGC regulates §4044. However, the IRS said an amendment causing an increased reversion could violate the "exclusive benefit rule" per Reg. 1.401-2(b)(1) (and this question has been incorporated into IRS materials used by agents reviewing determination requests upon a plan termination). The regulation says a reversion can only result from "erroneous actuarial computation", not a plan amendment decreasing benefits. Thus, you might increase some other benefit to keep the reversion from increasing due to the amendment. Suppose with the enactment of RPA, a plan is amended to decrease lump sums. This can be very helpful in making a plan sufficient enough to terminate. However, if this causes a plan to have a surplus (or a greater surplus, for plans that already had one) it may not be available for reversion to the employer until 5 years later. This was the decision in *Ramsey v. Northbrook, Inc.,* 1997 U.S.Dist. LEXIS 5475 (N.D.Cal. 3/12/97). Although not tested in court, you might suggest there was an actuarial error, since the actuary could not predict a decrease in minimum lump sums due to RPA94.

Several courts have concluded that if a plan document specifically stated, at one time, that any excess assets are to be used for additional benefits for plan participants, and if the document specifically restricted the employer's ability to amend that provision, then the employer may not amend the plan to provide that those excess assets will instead revert to the employer. Bryant v. International Fruit Products Company, Inc., 793 F.2d 118 (6th Cir. 1986); Delgrosso v. Spang & Co., 769 F.2d 928, 6 EBC 1940 (3d Cir. 1985) ; Rosenbaum v. Davis Iron Works, 669 F. Supp. 813 (E.D. Mich. 1987); 871 F.2d 1088 (6th Cir.

1989); cert. denied. Other cases permitting pension amendments to allow payment of excess assets to the employer upon plan termination involved plans that had not specifically required the use of excess assets to pay for additional benefits. Pollock v. Castrovinci, 622 F.2d 575, 1 EBC 2091 (2nd Cir. 1980); Washington-Baltimore Newspaper Guild v. Washington Star Co., 555 F. Supp. 257, 3 EBC 2609 (D.D.C. 1983) and In re C.D. Moyer Co. Pension Trust, 441 F. Supp. 1128, 1 EBC 1363 (E.D. Pa. 1977).

Government agencies which are interested in reversions are:
(1) IRS - wants to collect excise tax
(2) PBGC - the distribution is not complete until a legal reversion has been made
(3) Government contractors such as Medicare, Department of Defense and Department of Energy may want some of the reversion.

Contributory Plans

If the plan had employee contributions, then upon termination the portion of the residual assets attributable to employee contributions is to be Aequitably@ distributed to the employees who made such contributions (or their beneficiaries) per ERISA 4044(d)(3). The old PBGC regulations 2618.31 and 2618.32(b) specified the calculation as follows: (the new reg 4044.30 reserves a space for a rule, but is currently left blank)

$$\text{Residual Assets} \times \frac{\sum_{\text{all ees}} \text{PC2}}{\sum_{\text{all ees}} (\text{PC2 through PC6})} \times \frac{\text{ee PC2}}{\sum_{\text{all ees}} \text{PC2}} = \frac{\text{ee PC2}}{\text{PC2 through PC6}}$$

If participating annuities are used, a non-par bid will be needed to determine the residual assets.

Other alternative formulas were permitted for contributory plans in the past, but OBRA87 mandated the use of only the above formula per 4044(d)(3).

OBRA87 also mandated that participants who received lump sums or irrevocable commitments within the 3 years prior to DOPT also be included in the above fraction. Thus, those participants will get some of the residual assets. A PBGC notice of revised termination rules states that these amounts are determined as of the date of distribution. If the former participant received a lump sum, then their PC2 amount equals their employee contributions with interest up to the date of distribution of the lump sum and "PC 2 through 6" equals the amount of their lump sum. If the former participant received an annuity, then his/her PC2 amount equals the present value of their EEC benefit plus the present value of the death benefit refunding EEC upon death) and "PC2 through PC6" equals the purchase price of the annuity. Evidently, this 3 year look back does not apply to non-contributory plans which have reversions (see the first sentence of 4044(d)(3)).

There are questions as to how PC2 is determined for retirees in the above formula. Are EEC the "first out" payments (see ERISA 4044(b)(5) and the preamble to the 1976 interim reg 2608) or are they paid out proportionately with the employer-provided portion? TRA86 changed this for purposes of how much of a retiree's benefit is taxable. Pre-TRA86, the 3-year rule allowed all of the initial payments as a non-taxable return of EEC (if they could be paid out in 3 years). TRA86 says every retiree payment is part return of non-taxable EEC and part taxable employer-provided benefit. Should this new rule apply to the determination of PC2 in the above formula? Your retirees may think so, especially since they could not deduct all of their earliest payments as if they were EEC. This problem becomes clearer if a plan has

only retirees who have been retired for over 3 years (and thus have probably had total payments in excess of their employee contributions). The old rules would say they receive none of the residuals. If the residual rule followed TRA86 tax law and if the employees had contributed say 25% of the contributions, then they would get about 25% of the residuals. In a recent case with a pre-OBRA87 termination date, the retirees of Amalgamated Sugar claimed just that; that they contributed about 25% of the contribution and should receive about 25% of the reversion. Amalgamated Sugar's plan administrator used the presumptive rule (PC2 / PC2 through 6) where participants retired for over 2 years had PC2 = 0 because EEC were drawn down by the full benefit distribution. This calculation gave the retirees less than 1% of the reversion. The judge said this was not "equitable" per 4044(d)(3)(A) in Holland v. Amalgamated Sugar Co. (in US District Court, District of Utah, Central Division) 14 EBC 2292. The Tenth Circuit agreed for plaintiffs and remanded back to the District Court for a recomputation of the amounts due to retirees. (Holland v. Valhi Inc., CA 10, 22 F.3rd 968, 1994 US App LEXIS 8244, 92-4183, Nos. 92-4049/4054, 4/19/94). Plans can avoid this by subtracting only the portion of the distribution attributable to EEC (a la TRA 86). This would probably seem more "equitable" to retirees.

The old Part 2618.32(c) and Revenue Ruling 80-229 remind us that the allocation of excess assets in integrated plans to employees must not violate the maximum integration spreads. Compliance with integration rules can be achieved either by amending the plan formula before termination to absorb the excess, or by allocating all or a portion of the excess, as necessary, based on a non-integrated formula.

What if an employer eliminates the surplus by improving active employee benefits in a plan that was contributory? Some of those employee contributions came from the current retirees. Do they deserve some of the surplus? The retirees of Great Northern Nekoosa Corporation thought so when GNN used up the surplus by amending the plan to immediately vest and improve benefits of active employees upon takeover (to fend off a hostile takeover by Georgia Pacific). The 7th Circuit allowed the GNN amendment and stated that "the retirees do not own the [surplus] assets...but a promise of benefits." (Johnson v. Georgia Pacific Corp., CA 7, No. 93-2357, 3/23/94). A similar decision was made in the Third Circuit in Malia v. General Electric (23 F. 3d 828, 18 EBC 1113, 1994) when a merger reduced the amount of surplus, and thus, the portion attributed to employee contributions.

Other ways to use up surplus are discussed in the Reversion section of Chapter III.

PBGC PRIORITY CATEGORIES - Section 4044: Allocation of Assets

PC 1 Voluntary employee contributions

PC 2 Mandatory employee contributions

Basic = PBGC pv of ee portion of NRB + pv of return of ee contributions upon death
NonBasic = Total ee contributions less Basic PC 2
= $0 if EEC not withdrawn

PC 3 Benefits in pay status 3 years before DOPT or that could have been, using plan provisions in last 5 years under which benefits would be the least.

PC 4 Guaranteed Benefits

equals accrued benefits reduced to the maximum and then reduced by a phase-in of any benefit increases in the 5 years prior to DOPT
Substantial Owner (S/O) benefits are phased-in over 30 years
PLUS S/O benefits up to the regular guarantees and benefits in excess of the multiple plan aggregate payments limitation

PC 5 All non-forfeitable benefits (except those becoming non-forfeitable because of plan termination or earlier partial termination)

This includes: subsidies in optional forms for vested employees subsides in lump sums for vested employees QPSA (a charge can be made for it) for vested employees automatic COLA's which are scheduled post-DOPT for vested employees. But does not include: early retirement subsidies contingent on future employment, future disability, death, shutdown benefits for which event has not occurred.

This category is allocated amendment by amendment from DOPT-5 to DOPT. If plan is under 10 years old, or benefits were improved materially within last 10 years, see IRS regulation 1.401(a)(4)-5(b) and Rev. Rul. 80-229 (Benefits of top 25 HCE may be limited to a straight life annuity).

PC 6 "All other benefits under the plan" includes:

- the non-vested portion of benefits for those active on DOPT
- the subsidy in lump sums and other optional forms for non-vested employees
- Early retirement subsidies contingent on future employment (if employee remains employed long enough to get it)
- Benefits contingent on future events such as disability, death and supplements which are not protected by 411(d)(6), can be removed from plan. If not removed, they are in PC 6.
- the Blessit decision of the 11th Circuit said that future accruals are in PC 6, but was overturned en banc
- The benefits of separated, non-vested employees might be in PC 6 (unless employee is deemed cashed out under plan rules)
- The non-vested portion of benefits of partially vested separated employees might be in PC 6 (unless employee is cashed out under plan rules)
- If employee took irrevocable commitment, but employer still is the contract holder, the employee could become fully vested at DOPT.

Reversion attributable to employee contributions

$$\frac{\text{PC2}}{\text{PC2 through PC6}} \times \text{market value of residual assets (based on non-par bid)}$$

Include all those who got a lump sum or irrevocable commitment within 3 years before DOPT.

Any amendments that reduce the percent of reversion due to employees cannot go into effect for 5 years.

Minimum Lump Sums – §§411(a)(11) and 417(e)

Plan lump sums can not be less than PV of NRB, using 417(e) rules. See 1.417(e)-1 and 1.411(d)-4, Q&A#2. The employee must be informed of the relative values in case the lump sum is less valuable than the pension including any early retirement subsidies. If the plan document has a larger lump sum it cannot be cut back on past accruals. An immediate QJSA must be immediately available also and must be the most valuable option.

VIII. EMPLOYER LIABILITY TO THE PBGC (OR PLAN)

1. Single Employer Plans

ERISA §§4062, 4063 and 4064 impose a liability upon Contributing Sponsors (and each member of their Controlled Groups) to be paid to the PBGC in the event of plan termination or in the event an employer withdraws from a multiple-employer plan.

A **Controlled Group** (CG) generally includes any (a) Parent corporation, proprietorship, partnership, trust, estate, or other entity which owns 80% or more of the value or votes of the sponsor, and (b) any Brother/Sister corporation (or subsidiary of such) which a parent owns at least 80% of. A Parent Corporation cannot diffuse ownership by splitting the owners into 5 entities - the PBGC will aggregate them. Partnerships that are in the CG make each Partner liable. Incorporation will protect the individuals from the liabilities of the corporation, unless fraudulent activities occur (or unless the corporation is undercapitalized per State law), whereupon PBGC may "pierce the Corporate Veil."

The liability is **"Joint and Several"** which means that each member of the controlled group owes the whole amount (although the PBGC will not collect more than the full amount, and usually collects far less, from all of the controlled group members). Individual shareholders, officers, and directors (as such) are generally not personally liable under ERISA but Partners could be.

The employer liability equals the plan's unfunded benefit liabilities. This liability can be broken into 2 parts: the portion owed to the PBGC for their guarantees (the unfunded guaranteed benefits) and the portion owed to the participants to cover their benefit cutback. This second portion is called the outstanding benefit liabilities and is also owed to the PBGC. (PBGC puts in a claim for its losses and participants' losses, and shares its recoveries with participants in accordance with ERISA section 4022(c).) It equals the value of the benefit liabilities in excess of the benefits paid by the PBGC through both its guarantees and the asset allocation on DOPT. Before discussing PBGC's specific claims, it is valuable to discuss some general bankruptcy information.

Important Bankruptcy Terms

Prepetition:	Before date of bankruptcy filing (DOBF)
Postpetition:	On or after DOBF
Chapter 7:	Liquidation in Bankruptcy
Chapter 11:	Reorganization through Bankruptcy (sometimes liquidating if reorganization doesn't work)
Liquidating 11:	This is where employer uses the Chapter 11 Reorganization process to keep control of the liquidation
Contract rejection:	Contracts can be broken while in bankruptcy in order to reorganize. The aggrieved party hurt by the contract rejection gets a claim, on which they may or may not collect anything. In 1986, LTV rejected its promises to retirees by eliminating their Retiree Health plan. Subsequently, Congress passed a law prohibiting bankrupts from doing this on Retiree Health, Life, and Disability plans.

Preferences: When someone gets paid within 90 days prior to DOBF (or "Insiders" within one year before DOBF). These amounts may be recoverable by the bankruptcy estate and distributed "more equitably" per the Bankruptcy Code among many claimants. Are **payments to the pension** plan preferences (especially since the HCE's who benefit from the plan are Insiders)? Recent bankruptcy legislation suggests no.

Automatic Stay: Rule to leave company alone while in bankruptcy. The Government is sometimes excepted for regulatory or policing purposes. For example, the PBGC can involuntarily terminate or restore a plan while company is in bankruptcy, but PBGC can't perfect its liens against a company in bankruptcy for missed minimum contributions to the pension plan.

Bankruptcy Priorities

Who gets the remaining assets in a bankruptcy? This is governed by Section 507(a) of the Bankruptcy Code of 1979 as amended through 2005. A synopsis is as follows, in order of priority:

A. Secured Assets/Liens - a right to the property of the debtor.
B. Priority Unsecured Claims.
   (1) Administrative. Needed to administer company post-DOBF.
   (2)
   (3) Wages up to $4,925 per employee for the 90-day pre-DOBF period.
   (4) Benefits up to $4,925 per employee for the 180-day pre-DOBF period minus priority (3).
   (5)
   (6)
   (7)
   (8) Certain tax claims.
C. General Unsecured Claims - everything else.

PBGC Claims

a. ERISA 4062(b): UBL - applies to single-employer (S-E) plans. The employer (*i.e.*, the contributing sponsor and each member of the controlled group) maintaining the plan is liable upon plan termination for the unfunded benefit liabilities. Section 4068 gives the PBGC a lien (which has higher priority in bankruptcy if it is perfected pre-DOBF) of up to 30% of the sponsor's and controlled group's collective aggregate positive net worth. Net worth is determined under 4062(d) and can be determined at any point in time chosen by the PBGC during the 120-day period ending on DOPT. The PBGC may argue that the remainder of the UBL claim is post-petition with highest priority, if the plan terminated on or after DOBF.

b. ERISA 4062(c): DUECs The PBGC (as plan trustee) has a claim for Due and Unpaid Employer Contributions (DUECs). PBGC argues that its DUEC claims for periods after the sponsor's bankruptcy filing date should receive the highest (administrative) priority for unsecured claims under §§507(a)(1) and 503(b)(1)(A) & (B) of the Bankruptcy Code. However, the 6th Circuit disagreed with respect to the non-normal cost portion in In re Sunarhauserman, Inc., 126 F.3d 811 (6th Cir. 1997). The non-normal cost component of DUEC's for the 180 days prior to the bankruptcy filing (or cessation of business, if earlier) may have fourth priority under 507(a)(4). Frequently a sponsor of a plan undergoing Distress Termination will not hire an actuary to determine this DUEC, so the PBGC will determine it. The PBGC generally continues to use the prior plan actuary's assumptions, but has on occasion changed them, if they were too liberal. The PBGC also initiated a suit against an actuarial firm, for underpredicting the possibility of a plant shutdown (and not disclosing such). All outstanding balances of waivers and those unpaid balances due to extensions of amortization periods are added to the DUEC claims. The portion of this claim determined to be collectible is added to plan assets before the 4044 allocation. Note: Per Revenue Ruling 79-237, 412 minimum funding rules will apply through the end of the plan year following DOPT, with appropriate proration to reflect only the portion of charges and credits before DOPT. Non-payment of a deficiency could result in the imposition of the 10% excise tax and, subsequent to a notice, the 100% excise tax. Revenue Procedure 95-51, Section 4.03 allows for automatic approval of change in funding method to unit credit, as long as the market value of assets exceed benefit liabilities and the Schedule B has not been filed (or is not past due).

c. IRC Section 412(n): Missed Contribution Liens - provides PBGC the ability to perfect a lien on the contributing sponsors (and each controlled group member) equal to the smaller of:

(1) unpaid contributions with interest, or
(2) unpaid contributions with interest for plan years 1988 and later.

The contributing sponsor or the ultimate parent of the controlled group must use PBGC Form 200 to notify the PBGC within l0 days if the total of unpaid contributions (including interest) exceeds $1M. The form provides PBGC the information needed to perfect its lien. To the extent this lien is not perfected (or the collateral is insufficient to cover the claim), the PBGC may claim entitlement to an administrative tax claim (first priority of unsecured claims) for the portion falling due post-petition (after bankruptcy filing date). To the extent they are pre-petition, the PBGC may claim they fall in the 8th priority for unsecured tax claims. However, the courts have rejected these PBGC arguments. See, e.g., In re CSC Indus., Inc. & Copperweld Steel Co., 232 F.3d 505 (6th Cir. 2000); In re CF&I Fabricators of Utah, Inc., 150 F.3d 1293 (10th Cir. 1998).

In 1994, RPA gave the PBGC concurrent authority to enforce minimum funding rules if missed contributions exceed $1M, whether a company is in bankruptcy or not (and whether the plan is being terminated or not).

d. IRC 412(f)(3): Waivers The IRS requires security to the plan as a condition for getting a waiver where the waived amount is $1M or more, and often has the PBGC negotiate the terms of the security. The PBGC has the authority to perfect and enforce the security interest.

e. ERISA 4062(e): Facility closing If an employer ceases operations a facility and more than 20% of its participants are separated, the employer can be treated as a substantial employer as if under sections 4063, 4064, and 4065. The PBGC has started using this authority to get cash (in escrow) or security for the plan equal to a portion of the plan's total underfunding on a termination basis.

f. ERISA Section 4063: Withdrawing from a Multiple Employer plan: Section 4063 applies to withdrawals of an employer in S-E plans with more than one contributing employer (not under common control). A substantial employer (i.e., making 10% or more of the contributions) is liable for an escrow payment of its pro-rata share (based on contributions over 5 years) of the plan's 4062 liability in the event the employer withdraws from the plan. In lieu of paying this liability into escrow, the employer may be required to post a bond for 150% of the liability. If the plan continues for 5 years after withdrawal, the liability is abated and any payments held in escrow are refunded without interest (or the bond is canceled).

g. ERISA Section 4064: Terminating Multiple Employer plans: Section 4064 applies to terminating S-E plans with more than one contributing employer (not under common control). In the event of plan termination, the unfunded benefit liabilities owed to the PBGC are prorated over all employers based on contributions made during the 60 months prior to termination. The DUEC liability is spread over the employers on an equitable basis.

h. ERISA Section 4069: Transactions to Evade Liability – Under ERISA section 4069, if a principal purpose of a person in entering into a transaction is to evade liability, and the plan terminates within 5 years after the transaction becomes effective, the person (and its controlled group members) may be held liable as if they were the contributing sponsor of the plan at the time it terminates.

Navistar (formerly known as International Harvester) sold its Wisconsin Steel Division to a weak buyer (Envirodyne), which several years later terminated the steel division's drastically underfunded plan. The courts held that Navistar could not avoid liability in this manner (PBGC v. Envirodyne Industries, Inc., US Dist. Ct., 10 EBC 1458, 11/16/88), and SEPPAA added 4069 effective 1/1/86 to clarify this issue.

In another case (PBGC v. White Consolidated Industries Inc., CA 3, No. 92-3676, 6/30/93), White Industries (the seller) denied liability to the PBGC because Blaw Knox Corp. (the buyer) failed more than 5 years after White Industries sold a group of unprofitable steel companies to them. Blaw Knox paid no money for the steel companies' assets, but did assume their liabilities. White Industries knew that Blaw Knox could not meet its new pension liabilities, so they agreed to contribute $4 million annually to the plans for almost 5 years. The court agreed with the PBGC that the 5 year limitation in 4069 starts when the seller stops supporting the plan, not the sale date, and thus White Industries was liable.

i. ERISA Section 4071: Penalty for Late Information - the Pension Protection Act also allows the PBGC to assess a penalty of up to $1,000 per day (increased since then for inflation to $1,100 per day) for failure to provide a variety of PBGC-related notices and disclosures, including reportable events, Form 200 filings, annual employer reports under ERISA section 4010, premium-related information submitted as part of the annual premium filing, and Participant Notices under ERISA section 4011.

j. ERISA 4007(c) & (e): PBGC Premiums: The PBGC may bring a civil action to recover premiums, penalties, and interest against the contributing sponsors and each member of their controlled groups. The claim is joint and several.

Establishment of the Plan Termination Date The termination date is important for a number of reasons. The employer's minimum funding obligation continues until the termination date. Benefit accruals continue until the termination date (absent a prior freeze), and in some plans, additional benefit liabilities can be triggered by events that occur prior to termination, such as a plant shutdown. Participants can benefit from later DOPTs because they can become eligible for early retirement subsidies. On the other hand, other participants can lose the termination benefit if they separate (with a

deemed cash out) or die without a spouse before DOPT. The termination date can affect the extent of the PBGC's benefit guarantee, because the PBGC maximum guarantee increases each year, and because benefit increases made within the five years before termination are phased in at 20 percent per year. The termination date can affect the extent of the employer's liability for unfunded benefits. Interest rates for valuing plan benefit liabilities are determined as of the date of plan termination. In addition, the identity of the liable employer and the extent of any priority claim that PBGC may have may be determined as of that date. In an involuntary termination by PBGC, the termination date will be set no earlier than the date participants have effective notice that they are no longer accruing benefits, but may be set later if a later date is financially advantageous to the PBGC.

Determining the Amount of PBGC's Claim in Bankruptcy An important question is whether PBGC regulations control in bankruptcy for purposes of setting the interest assumption to determine the present value of PBGC's termination liability claims. Two circuits of the Court of Appeals have ruled against the PBGC, holding that a "prudent investor" rate should be used. See In re CF&I Fabricators of Utah Inc., 150 F.3d 1293 (10th Cir. 1998), cert. denied, 526 U.S. 1145, 143 L. Ed. 2d 1032, 119 S. Ct. 2020 (1999); In re CSC Indus. Inc., 232 F.3d 505 (6th Cir. 2000), cert. denied, 534 U.S. 819, 151 L. Ed. 2d 20, 122 S. Ct. 50 (2001). However, in a more recent decision, a Bankruptcy Judge "respectfully disagreed" with these decisions and upheld the PBGC's position that its interest assumptions should apply in bankruptcy. See In re US Airways Group Inc., 303 B.R. 784, 792 (Bankr. D. Va., 2003). Note that the PBGC's valuation regulation assumptions are designed to replicate private-sector group annuity pricing and base the interest assumptions on a survey of that pricing. PBGC effectively "solves" for an interest factor that, when combined with the mortality assumptions prescribed in its valuation regulation, best replicates the survey results across a range of ages. The PBGC updated its mortality assumptions in 1993 (from UP-84 to GAM-83, with the effect of increasing its derived interest assumptions. In March 2005, the PBGC proposed another mortality update (from GAM-83 to GAM-94 Basic projected to the year of the valuation plus 10 years); if and when this proposal is finalized, there will be another increase in PBGC's interest assumptions.

2. Multiemployer Plans

In multiemployer plans, employers that completely or partially withdraw are responsible for their share of unfunded vested liabilities (not unfunded guaranteed liabilities or unfunded benefit liabilities). Payments toward this liability are made to the plan for 20 years, or until the employer's liability is fully amortized, if earlier. The amount of the liability is adjusted by:

(a) a de minimis reduction,
(b) a reduction to reflect if the withdrawal is partial,
(c) a limitation due to the maximum of 20 years of payments, and
(d) a percentage similar to the 30% of net worth in S-E plans (only used in certain situations).

Each plan must set the "reasonable" actuarial assumptions for the determination of the vested liability.

De Minimis Example - If the unfunded vested liability (UVB) allocated to an employer is so small that it is less than the smaller of 3/4 of 1% of the plan's total UVB and $50,000, then the employer has no withdrawal liability to the plan because of the de minimis rule. If the employer's portion of UVB is greater than the de minimis amount but less than $100,000, their liability is reduced by the de minimis amount. The de minimis amount is phased-out dollar for dollar above $100,000. Note: the UVBs are both determined as of the last day of the plan year preceding the plan year in which the withdrawal occurs. A discretionary de minimis rule can be selected which changes the above dollar amounts.

For more on multi-employer plans, see Multi-employer Retirement Plans: Handbook for the 21st Century" by Dan McGinn which can be obtained at www.actuarialbookstore.com or 800-582-9672.

Outline of Multi-Employer Rules

4022 Single Employer guaranteed benefit rules.

4022A Multi-Employer (M-E) plan guarantee rules. See separate page in Chapter V of this Study Note.

4041 Only applies to Single Employer plans. It requires that assets cover all Benefit Liabilities. This does not apply to M-E plans.

4041A Applies to M-E plans. It says termination results from:
(1) mass withdrawal, (2) a freezing amendment, or (3) transfer to DC plan.

4044 Does not apply to M-E plans

4231 **Mergers & Transfers between M-E plans must:**
(1) Notify PBGC within 120 days before
(2) No reduction in Accrued Benefits
(3) Benefits may not be reasonably expected to be suspended - 4245
(4) Recent valuation must have been performed

4245 **Insolvent** = Assets < 1 year's benefit payments
Resource Benefit Level = level of benefits that can be paid from available assets
Insolvency Year = Plan Year in which plan is insolvent
Benefits must be reduced to Resource Benefit Level (or Basic Benefits if greater)

4241 **An M-E plan is in Reorganization if:**

Reorg.Index = $UVB_{retirees} / \ddot{a}_{10\neg}$ + $UVB_{non\text{-}retirees} / \ddot{a}_{25\neg}$ - MinContribution > 0

Then, contribution must be increased per 4243 or benefits decreased per 4244A (but not below basic benefits).

4244 **Overburdened Plan** = plans with # retirees > # actives, & contribution rates are up.
Plan gets to reduce Min Cont by Overburden Credit = 2 x AvgGuarBen x (#retirees - #actives)

This is a rough outline. Call Bob Rideout x 3357 for more details.

4211 Withdrawal Liability (WL) calculations: (determine as of last day of prior plan year)

Presumptive Method:

WL = $\underline{TotUVB_{9/80} \times [1- 5\% \times \text{yrs later}] \times \quad \text{ER's required contributions over last 5 years}}$
Total Actual Contributions (excluding then-withdrawn ER contributions) last 5 years

$\pm E\ )UVB_t$ x " x " } different for each

$\pm E$ Reallocated UVB_t [16] x " x " } year since 1980

Modified Presumptive Method:

WL = $TotUVB_{9/80}$ x ($\ddot{a}_{15-t\rceil}$ / $\ddot{a}_{15\rceil}$) x "

+ (Total $UVB_{DeterminDate}$ - above amt - amts collectible) x "

Rolling 5 Method:

WL = [Total $UVB_{DeterminationDate}$ - amts collectible] x "

4209 De Minimis rule: Reduce above employer WL by:

Min[3/4% x $TotUVB_{EOPY\ before\ W/D}$, $50,000] - [(WL - $100,000) ⇔0] $50K phases out at $150K

or

Min[3/4% x $TotUVB_{EOPY\ before\ W/D}$, $100,000] - [(WL - $150,000) ⇔ 0] $100K phases out at $250K

Not applicable on Mass Withdrawal. Otherwise there would not be enough assets to pay benefits.

4205 Determination of Partial Withdrawal

A partial occurs on the last day of a plan year, if:

70% Decline Rule: Each year in 3 year testing period < 30% of Highest 2 of prior 5 years[17]

Testing period = Partial Withdrawal year and 2 *preceding* plan years

Retail Food Industry: Replace 70% with 35% and 30% with 65%.

Partial Cessation: Permanent cessation of portion

4206 Adjustment for Partial Withdrawals

Multiply WL on the withdrawal date by:

[1 - $ContribBaseUnits_{PlanYrAfterPartial\ Yr}$ / $AvgContribBaseUnits_{5\ PlanYrsBeforePartial\ Year}$

For 70% Decline Rule: Withdrawal Date = the last day of *first* plan year in 3 year testing period, and the denominator uses the 5 years before the 3-year testing period.

[16] Reallocated UVB arise from De Minimis reductions in Employer Liability per 4209, the 20-year limit on withdrawal liability payments per 4219(c)(1)(B), and the limit on employer liability as a percent of liquidation value (after sale).

[17] The 2 years do not have to be necessarily consecutive years.

IX. REPORTING AND DISCLOSURE

1. Reportable Events

ERISA 4043 mandates that the plan administrator and each contributing sponsor of a covered single-employer plan must report certain events to the PBGC (not employees) in order for the PBGC to protect participant's benefit rights and the termination insurance program. In general, the filer must report these events within 30 days after he or she knows or has reason to know of the event unless the PBGC waives or extends notification. The reportable event forms and instructions are available from the website provided on the last page of this Study Note.. If the sponsor fails to provide a required notice, it may be subject to a penalty of up to $1,100 per day. A brief summary of the reportable events covered in regulation 4043 as well as the circumstances when notice is waived or extended follows.

Summary of Reportable Events Filing Requirements

Reportable Event	Circumstances when Notice Waived or Extended
1) Tax Disqualification or Title I Non-compliance	Always waived
2) Amendment decreasing benefits	Always waived
3) Reduction in Active Participants[18]	Waived if: - UVB < $1 M or no VRP or (using optional assumptions) no UVB or - MVA, 80% vested benefits and not a 4062(e) event - fewer than 100 participants (beginning of this year or last year) Various extensions tied to premium and Form 5500 due dates
4) Termination or partial termination	Always Waived
5) Failure to make required minimum funding quarterly or other payment	Waived if: - payment is made within 30 days of its due date; or - Missed quarterlies do not need to be reported for small plans (<100, or <500 and no 4011 Notice required) per Technical Update 97-6 NOTE: Filing of **Form 200** with the PBGC within I0 days detailing an underfunded plan's non-compliance with

[18] Actives in plan < 80% at beginning of year, or < 75% at beginning of prior year. PBGC can apply 4062(e) here. See the prior chapter on this.

		minimum funding (unpaid contributions with interest > $1,000,000) satisfies the reportable events requirement (Form 200 helps the PBGC perfect its lien under 412(n))
6)	Inability to pay benefits when due or liquid assets< 2 x disbursements	Waived unless plan has < 100 employees
7)	Distribution to a substantial owner ($10,000 or more, 10% owner, not a death benefit, and after distribution there are unfunded nonforfeitable benefits)	Waived if -Distribution 415(b) max or 1% of plan's MVA, or -No VRP, no UVB using optional assumptions, MVA -80% vested benefits -Due date may be extended to 30 days after premium filing
8)	Merger, consolidation, transfer	Always Waived, however see (9) and (12) below
9)	Loss of a controlled group member (includes transfer of plan to other CG or liquidation of sub into parent[19])	Waived if: - Leaving sponsor is 10% of Controlled Group (CG) or a foreign entity (other than a foreign parent), or - No VRP, UVB < $1M, or (using optional assumptions) no UVB - Public company and MVA 80% vested benefits Due date may be extended until 30 days after Form 1 filing
10)	Liquidation or proceedings to liquidate (including liquidating into another CG member)	Waived if: - Same as above (funding-based waivers require that plan be maintained by another member of CG)
11)	Extraordinary dividend or stock redemption (even if within CG) > net income or > 10% of total net assets (see reg for definitions)	Waived if: - person making distribution is no more than 5% of CG, foreign entity other than foreign parent, or is foreign parent and distribution made solely within CG - otherwise same as (9)
12)	Transfer of Benefit Liabilities outside controlled group (including spinoffs)	Waived if: - all of plan's assets and liabilities are transferred, - de minimis transfer, or - transfer complies with 414(l) using PBGC safe harbor assumptions - transfer complies with 414(l) and resulting plans are fully funded on PBGC basis
13)	Application for Minimum Funding Waiver	Never Waived

[19] If a company with little debt is liquidated into the parent (or its assets are sold and proceeds are upstreamed), and the parent has significant debt that would compete with the PBGC's employer liability claim, PBGC's ability to collect on claim is harmed, given its unique ability to pursue that liability on a joint and several basis against each controlled group member.

14) Loan default (by member of CG) if balance at least $10M and non-payment not corrected within 30 days, and in other prescribed circumstances (see reg for details)	Waived if: - default cured, or - No VRP, UVB < $1M, or (using optional assumptions) - no UVB - foreign entity (other than a foreign parent) - Public company and MVA 80% vested assets Due date may be extended until 30 days after Form 1 filing or to one day after cure period expires, acceleration date, or notice of default
15) Bankruptcy, insolvency or similar settlements of CG member	Waived if: - foreign entity (other than a foreign parent)

Since the 30-day reporting requirement satisfies the PBGC's need, reporting in the Annual Report has been waived.

Advance Reporting: In privately-held firms (i.e., companies that don't file with SEC) with plans that have aggregate Funding Ratios (FR) <90% and aggregate Unfunded Vested Benefit (UVB) > $50M, the contributing sponsor that experiences the following events must notify the PBGC 30 days in advance of the effective date of the event on Form 10-Advance. The determination of aggregate UVB and aggregate FR includes all plans in the CG except plans with UVB $0. (Don't subtract the credit balance from assets. Calculate UVB using the general rule method used in calculating PBGC variable premiums.)

Reportable Event	Waived if:
9) Loss of Contributing Sponsor	Transferred plan has ≤ 500 participants, or Member ≤ 5% of CG
10) Liquidation	Member ≤ 5% of CG
11) Extraordinary Dividend or Stock Redemption >10%	Member ≤ 5% of CG
12) Transfer of Benefit Liabilities (Includes spinoff)	All assets and liabilities are transferred, or Transfer is de minimis, or Transfer meets 414(l) using PBGC assumptions and the benefits of ≤ 500 participants are transferred. transfer complies with 414(l) and resulting plans fully funded on PBGC basis
13) Application for Minimum Funding Waiver	Notice extended until 10 days after event
14) Loan Default (unless paid within 10 days)	Cured/waived within 10 days or by end of cure period Notice extended until 10 days after event
15) Bankruptcy or similar event	Notice extended until 10 days after event

All of the filed material is exempt from Freedom of Information Act (FOIA) disclosure rules. Multiemployer plans are not subject to the reportable events rules because the PBGC has waived reporting for them.

2. Notice to Participants in Underfunded Plans - ERISA 4011 and 29 CFR 4011

If a variable-rate premium is payable for a plan for a plan year, the plan administrator must provide participants with a Participant Notice for that plan year unless the plan meets a "DRC Exception Test" for the plan year or for the prior plan year. The DRC exception test tracks the gateway test for the DRC, i.e., it is met for a plan year if the plan has a funded current liability percentage for that plan year of at least 90%, or at least 80% with a percentage of at least 90% for two consecutive plan years out of the three preceding plan years. The Participant Notice provides participants with information about the funding level of the plan on a current liability basis, and also provides information about the PBGC's guarantee and its limits. The notice is due at the same time as the Summary Annual Report for the prior plan year, i.e., two months after the due date (or extended due date) of the Form 5500 for the prior plan year. The Participant Notice may be sent in the same envelope as the SAR, but must be a separate document. See PBGC regulations at 29 CFR Part 4011 for more details. Each year, the PBGC publishes a Technical Update that includes guidance on Participant Notice requirements and provides a model notice. It should be noted that the plan administrator must certify in the annual premium filing that they complied with this Participant Notice regulation.

3. PBGC's Early Warning Program

The PBGC monitors controlled groups with underfunded pension plans in order to identify corporate transactions that might jeopardize participants' retirement benefits or put the PBGC at greater risk. Because of their powers and threats, the PBGC has been able to negotiate deals with buyers and sellers that protect PBGC interests and the interests of the participants. See the section in the next Chapter right after "Spinoffs" called "PBGC Involvement" for more details.

4. Annual Financial and Actuarial Information Reporting to PBGC - ERISA 4010

Controlled Groups (CG) with aggregate UVB > $50 M or with waivers or missed contributions exceeding $1 M must file certain information annually with the PBGC. The following information is due by April 15 for CG's with calendar year FY:

(1) Identifying information for each entity (except entities under 5% of CG) and their relationships in the CG and for each plan in the CG, along with information about changes in the CG.
(2) Actuarial Valuations, Benefit Liabilities, Market Value of Assets, and certain other information that can help PBGC value plan liabilities (except for exempt plans with MVA > BL or less than 500 participants unless the plan has any missed contributions or waivers)
(3) Financial Statements for each entity (except entities under 5% of CG).
(4) Information about frozen plans.

In addition, if a filing was required for the prior year but is not required for the current year, the filer must still file for the current year to make a demonstration as to why filing is no longer required.

This information will help PBGC monitor the entities, their plans, and their transactions. Starting with the filings due (for calendar-year filers) on April 15, 2005, for the 2004 Information Year, 4010 filings must be submitted to the PBGC electronically. The information that is submitted is treated as confidential and disclosure is restricted.

X. MERGERS, CONSOLIDATIONS, SPINOFFS, AND TRANSFERS

Up to now, this study note has covered actuarial aspects of terminations under Title IV of ERISA. This final section will address the provisions of the Internal Revenue Code that deal with mergers, consolidations, spinoffs and transfers among plans. It is included in this Study Note because the requirements of the Code are based on the Title IV provisions governing plan terminations.

IRC 401(a)(12) and 414(l) and ERISA 208 require that a merger, consolidation, spinoff or transfer cannot occur if any participants could suffer a reduction in benefit on account of the merger, consolidation or transfer in the event of plan termination. Specifically, IRC 414(l) states:

"414(l) MERGERS AND CONSOLIDATIONS OF PLAN OR TRANSFERS OF PLAN ASSETS
(1) In general - a trust which forms a part of a plan shall not constitute a qualified trust under 401 and a plan shall be treated as not described in 403(a) unless in the case of any merger or consolidation of the plan with, or in the case of any transfer of assets or liabilities of such plan to, any other trust plan after September 2, 1974, each participant in the plan would (if the plan then terminated) receive a benefit immediately after the merger, consolidation, or transfer which is equal to or greater than the benefit he or she would have been entitled to receive immediately before the merger, consolidation, or transfer (if the plan had then terminated). The preceding sentence does not apply to any multi-employer plan..."

Note that a transfer of participants and assets from a multi-employer plan to a single employer plan must comply with 414(l).

Single Plans

Section 1.414(l)-1 of the Regulations, elaborating on 414, defines a "single plan", and is suggested reading. A plan is a "single plan" if and only if, on an ongoing basis, all of the plan assets are available to pay benefits to employees who are covered by the plan and their beneficiaries. For purposes of the preceding sentence, all the assets of a plan will not fail to be available to provide all the benefits of a plan merely because the plan is funded in part or in whole with allocated insurance instruments. A plan will not fail to be a single plan merely because of the following:

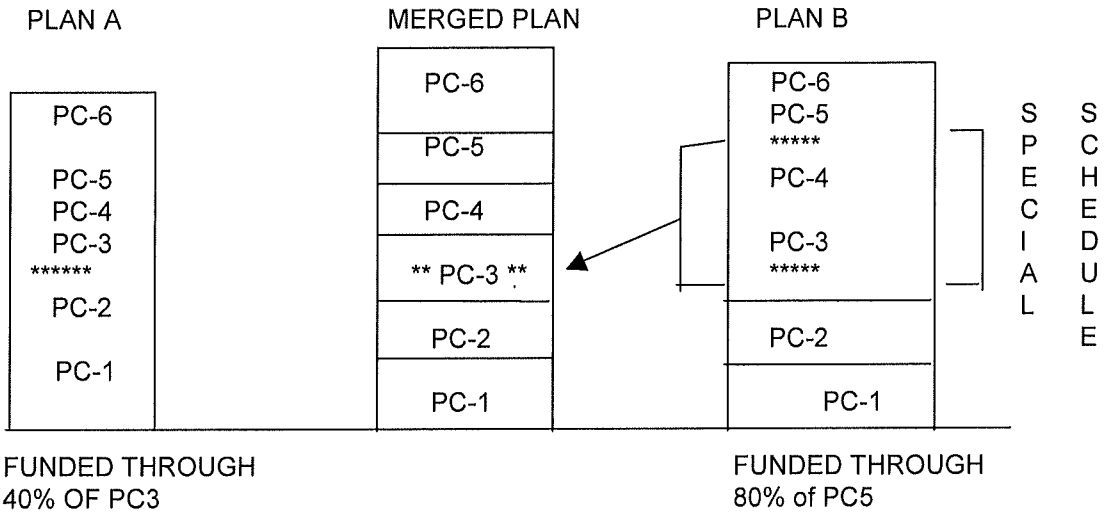
(i) The plan has several distinct benefit structures which apply either to the same or different participants,
(ii) The plan has several plan documents,
(iii) Several employers, whether or not affiliated, contribute to the plan,
(iv) The assets of the plan are invested in several trusts or annuity contracts, or
(v) Separate accounting is maintained for purposes of cost allocation but not for purposes of providing benefits under the plan.

However, more than one plan will exist if a portion of the plan assets is not available to pay some of the benefits. This will be so even if each plan has the same benefit structure or plan document, or if all or part of the assets are invested in one trust with separate accounting with respect to each plan. This definition has important implications for plan sponsors. For example, a company with several subsidiaries can have different pension provisions for each subsidiary and yet file a single consolidated annual report to the government (Form 5500). Having a single plan can be a detriment though. Suppose the plan is underfunded upon the sale of a subsidiary (with the plan transferred to the buyer). You will have to do a 4044 allocation of assets if it is a single plan. Such an allocation can be very complicated and time consuming (and hence expensive) to complete. Having a fully funded plan before the spinoff (or after the merger) will make it much easier to perform a spinoff (or merger) as it will be easy to ensure everyone maintains their full benefit. You will have to be careful if any of the plans gives surplus assets to employees.

The "Single plan" definition is now also used in other areas (e.g. 401(a)(26), 401(a)(4), and 410(b)). The next 2 sections discuss mergers and spinoffs. A transfer is just a combination of the 2 and needs to comply with both sets of rules. One note: you will find the transactions much easier to perform, FAS88 curtailments and settlement accounting, and the filings of the IRS Form 5310-A and PBGC premium Forms 1 much simpler if the transaction date is the first day of the plan year. Assets don't have to move on the date of the merger or spinoff. The effective date is based on facts and circumstances per the IRS, but generally is the date that service or accruals start in the other plan. The Form 5310-A should be filed 30 days in advance, but if not timely, only a $25 per day penalty is due, per the Instructions to the Form. You will note that the Instructions for Item 4a and 4b state that the actuarial statement of valuation showing compliance with 410(a)(12) and 414(l) does not need to be signed by an actuary.

Mergers

If the assets of a merged plan are sufficient to cover all accrued benefits, 414(l) is automatically satisfied. Otherwise, the merged plan must provide for a special schedule of benefits to insure that 414(l) is met. This Special Schedule will be needed if the plan later has a spinoff and is still underfunded. In addition, the PBGC will need this special schedule if the plan later terminates in an underfunded situation. The following chart illustrates how an altered 4044 allocation is performed after the date of a merger per 1.414(l)-1(f) when assets are not sufficient to cover all benefits.



Plan A is the lower funded plan. It is funded 40% into PC3, while plan B is funded 80% into PC5. The Special Schedule of accrued benefits (found in PC3, 4 & 5 at the merger date in Plan B) ensures that a 4044 allocation on the day after the merger will produce the same benefits as if done the day before the merger, thus complying with 414(l)(1). To create the special schedule for the example above:

(1) perform a §4044 allocation for the participants of Plan B as if the plan terminated immediately prior to the merger
(2) list each participant in Plan B along with his/her benefits in each priority category beyond the 40% level of PC3, but not beyond 80% of PC5.

If data sufficient to create the Special Schedule is maintained, then it is not necessary to prepare the schedule. Furthermore, the use of the schedule is no longer mandated after five years and the data mentioned above need not be maintained more than five years if the plan does not have a spinoff or termination.

After the merger, benefits will accrue and assets will change, but the Special Schedule will always remain at the 40th percentile of a 4044 allocation. Suppose one year later the merged plan had a spinoff (or terminated) and assets are no longer sufficient to cover the special schedule of benefits. (This can happen if the yield on assets is poor, or high priority liabilities increase more than the assets, or if contributions are less than post-merger accruals or when benefits that were not covered by assets are paid out.) Assets would then be allocated up to 40% of PC3 for everyone in the plan and then the scheduled benefits would be funded by allocating assets to the scheduled benefits as if there were no special schedule. (For example, some of the special schedule benefits which were in PC5 on the merger date, might now be in PC3.) Then the allocation would continue on the whole plan again starting at the 40.1% level of PC3.

Other considerations include successive mergers and the de minimis rule for merger of defined benefit plans. Successive mergers will potentially require the insertion of an additional special schedule. A de minimis rule exists for when a (smaller) plan whose liabilities (PV of accrued benefits[20]) are less than 3% of the (larger) plan's assets on at least one day in the plan year of the larger plan. In this situation, a special schedule of the smaller plan's 4044 benefits on a termination basis are put into Priority Category 0 (i.e. better than Priority Category 1) of the merged plan. If more than one merger occurs during the plan year of the large plan, then the de minimis rule applies only if the sum of the liabilities acquired is de minimis (i.e., less than 3%). The Form 5310-A is not needed for de minimis merges. Only mergers not processed under the non-de minimis rules need to be considered in determining whether the de minimis rules can be applied.

Several other items should be mentioned:

(1) After a merger, one or more plans will no longer exist. They should file their Final Form 5500 and check off a box saying they no longer exist due to the merger. The merged plan's Schedule B will then have the amortization bases and credit balances of the prior plans added together.

(2) For premium purposes, the PBGC has said that there will be no premium refunds when mergers cut a plan year short. However, practitioners have been able to get a refund by amending the plan to create a short plan year and then merging.

(3) If a plan being acquired has some unpaid minimum contributions, they of course, reduce the sale price. The acquiring company cannot pay them and deduct them as an ordinary and necessary business expense under IRC §§162 and 212. They are capitalized as part of the cost of the purchase and thus are depreciated (e.g., over 15 years). Future minimum contributions (including past service components per GCM 39274) can then be deducted.

(4) If anyone's accrual rates are reduced by a merger, a court said section 204(h) notices are needed or the reduction will be delayed (Koenig v. Intercontinental Life Corp., DC Pa., 1995 U.S. Dist. LEXIS 3309, 3/15/95). Thus, this ruling may affect the timing of the employer's action to merge plans and the effective date of the merger. See the discussion of the 204(h) notice in Chapter III.

Spinoffs When performing a spinoff, one must decide how much money to spin-off. It is important to read 1.414(l)-1(n) for spinoffs. If each spinoff plan is fully funded and each participant is allocated to one plan, then the spinoff easily complies with 414(l). (Private Letter Ruling 9142027 allowed the seller's plan to retain the early retirement subsidy. Either the buyer didn't want it or the seller thought the actual experience would be less than the additional assets that would have to be transferred with them.) De minimis spinoffs comply (and the Form 5310-A filing is not needed) if the assets spun off equal the PV of accrued benefits[21] spun off

[20] Is this different than the PV of benefits on a termination basis? Does it exclude early retirement subsidies? Regulation 1.414(l) -1 does not say.

[21] Ibid.

and if the total of such amounts is less than 3% of plan assets (on at least one day of the plan year). This works even if the parent plan is underfunded. Some people feel that annuity purchases exceeding 3% of plan assets should comply with the general rule so that the remaining participants aren't left with an empty trust fund. However, 1.414(l)-1(b)(4) and 1.414(l)-1(c)(1)(i) limit spinoffs to those with assets and/or liabilities moving between plans, not insurance companies (unless Section 414(l)(2)(f) is used by the IRS to include annuity purchases).

Prior to REA, a plan could eliminate early retirement subsidies for the spinoff participants and just spinoff the present value of the accrued benefit. The accrued benefit was a benefit commencing at NRA per 411(a)(7). When the service, but not the age, requirement for early benefits was satisfied before separation, Section 401(a)(14) indicated that actuarially equivalent early retirement benefits had to be available when the age requirement was subsequently reached. The court case Amato v. Western Union 773 F. 2d 1402, 1411(2nd Cir 1985) affirmed this and more. REA was passed to protect early retirement subsidies, just as accrued benefits at NRA were protected. It went further and said that post-amendment (or post-termination) service at the employer would count towards satisfying the age and/or service requirements for an early retirement subsidy. Revenue Rulings 85-6 and 86-48 confirmed that contingent early retirement subsidies are in benefit liabilities upon termination (if eligibility conditions are eventually satisfied) and that "termination" was an amendment for purpose of 411(d)(6). Thus, the actuary should consider these contingent benefits when determining the amount of assets to spin off. See Chapter VII, Section 6 for a more thorough discussion of contingent benefits and the "Same Desk" rule.

Section 414(l)(2) mandates that spinoffs within a controlled group must spread the old plan's excess assets over each participant's surplus. Each participant's surplus is defined as the difference between their Full Funding amount under 412(c)(7)(A)(i) and their present value of benefit liabilities. Otherwise, the parties involved could freely decide how much surplus goes to each plan. Section 414(l)(2) was probably created to limit the amount of plan surplus that a CG can take thru a spinoff-termination. (Of course, the CG can get around this by spinning off outside the CG.) When applying 414(l)(2), the formula breaks down if liberal actuarial assumptions (and method) cause the FFL to be less than the PV of benefit liabilities. Also note that if one spun off plan has all the actives, it can take all the surplus.

Other items to note are:

(1) The minimum funding rules for spinoff plans can be found in Revenue Ruling 81-212 and 86-47. They describe a reasonable method for how the amortization bases and credit balance can be split.

(2) A spinoff can accompany a partial termination of a plan (e.g, 20% of employees or more leave). This would accompany vesting of all employees spun off (i.e., the "affected" employees in 411(d)(3)).

(3) Don't forget to read the Joint Implementation Guidelines in Appendix B to see if they apply. If a spunoff plan terminates within 3 years, then the original plan may be affected.

(4) In order to avoid paying duplicative PBGC premiums, spinoffs could occur on plan anniversaries or one could amend the plan to have a short plan year end on the spinoff date.

Transfers

Regulation 1.414(l)-1 states that a transfer is a combination of a spinoff and a merger and must comply with both the spinoff and merger rules. Can the assets spun off be less than the liabilities spun off (as long as, per 414(l), funded benefits after the transfer were equal or greater than before the merger)? It won't comply with the regulation, but it does comply with the law. This happens all the time with transfers between hourly and salaried plans. Sometimes these transfers are implemented without any assets being moved - a naked liability transfer. A ruling by the National Office of the IRS hints that this is legal (LTR 9318035) and has been confirmed in informal discussions with the IRS. While the National Office doesn't rule on the qualification issues, such as whether the naked liability transfer complied with the exclusive benefit rule of

401(a)(2) or the transfer rules in 414(l), they did say that the use of one plan's surplus to cover the transferred liabilities from another plan, would not be deemed a reversion (subject to excise or income taxes), since the "transfer... is consistent with the use Congress intended under 404... when it granted the earlier deduction under 404. In this decision, the court relied on language in OBRA '87 that implied that there are "no income or excise tax consequences if excess assets are transferred or merged between DB plans by ...employers within the same controlled group. Thus, transfers of surplus to a DC plan or outside a controlled group could be deemed an indirect reversion and thus subject to the reversion excise tax. An earlier IRS Technical Advice Memorandum (TAM 9516005) helps with the exclusive benefit rule. It allowed an employer to transfer non-qualified supplements to an overfunded plan, saying it met the exclusive benefit rule, because the supplements were pension-type benefits and they were payable to "employees or their beneficiaries". The TAM also noted that, while the employer received an incidental benefit from the use of the surplus, it did not cause a prohibited transaction under IRC 4975, because it is for participants. Finally, to answer the 414(l) concern, it should be noted that the clear language of 414(l) itself contemplates a "transfer of assets or liabilities" (not and).

DOL also has concerns here. Actions involving pension plans by fiduciaries must be solely in the interests of participants. When a bank spun off an investment management division, it agreed to continue to use their services for the plans investments for an increase in sales price. This was held impermissible by DOL - also see DOL news release 97-82 (3/7/97).

PBGC Involvement

The PBGC monitors companies with underfunded pension plans in order to identify corporate transactions that might put participants or the PBGC at greater risk. In particular, the PBGC monitors spinoffs to ensure that they comply with 414(l) and its regulations, particularly if the spinoff creates a worse funded plan or goes to a weak buyer. PBGC reminded actuaries that 414(l) requires the use of termination assumptions to value the plan as if it were to terminate. Section 1.414(l)-1 allows PBGC assumptions as a safe harbor. In addition, PBGC was against using 30-year Treasury rates (by assuming many elect the RPA lump sum), unless participants had actually elected lump sums. This was especially true if the plan had no lump sum provision.

The PBGC has the power to involuntarily terminate the plan before spinoff through 4042(a) or make parties liable for plan underfunding (UBL, not just UGB) under 4069 if a principle purpose of the transaction was to evade pension liabilities. Other tactics used by the PBGC are:

(1) they sent a letter to SEC saying the spinoff documents filed with the SEC contained fraudulent numbers (i.e., they said the pension liabilities were very understated)
(2) they sent letters to possible debt lenders scaring them about the (understated) liabilities, the weakness of the buyer, and the possibility of PBGC action against the buyer to claim the UBL.

Because of these powers and threats, PBGC has been able to negotiate deals with the buyers and sellers for the following:

(1) more money to the spunoff plan (or security acceptable to PBGC - but this may affect the company's access to loans),

(2) making the seller (e.g., Pitney Bowes, Inc.) secondarily liable[22] for the pension underfunding in case the buyer or spunoff subsidiary (e.g., Pitney's subsidiary Dictaphone sold to Stonington) goes under within say 5 or 10 years, or until the buyer is financially strong (based on say credit ratings as good as the seller),

(3) have buyer (or really the stronger party) keep the underfunded plan, or part of it (the plan will then need to state how employees can grow into contingent benefits),

(4) merger of the underfunded plan with an overfunded plan,

(5) an agreement that PBGC will get all Valuation Reports, SEC filings (10 K and 10 Q), and notice of Participant drops of 20% or more,

(6) agreement that PBGC must consent to any changes in actuarial assumptions.

In a spinoff from a well-funded plan, PBGC (alerted by the Advance Notice) found that assets to be spun off were less than the value of benefits using PBGC assumptions. PBGC informed the plan's trustee (a bank) that the spinoff would not satisfy 414(l) - or more importantly ERISA 208 - which would make the Bank a violator of Title I's fiduciary standards. The seller then changed the spinoff enough to make PBGC happy. Now that PBGC has gotten the word out, they have said they may report actuaries who violate 414(l) termination assumptions rules to the ABCD. (Note that the actuary is not required by IRS to sign off on the assumptions.) PBGC's Chief Negotiations Actuary, Karen Krist, is available to discuss PBGC's view of an actuary's proposed assumptions if desired in advance.

Asset Buyer Beware

In Stock acquisitions the buyer acquires the liabilities of the acquired business, while the buyer of assets in an asset acquisition generally avoids them. Courts have created an exception to this when the buyer is deemed to be a successor employer (i.e., substantial continuity of business) and knew before the sale about the seller's potential liability (i.e., they could have protected themselves by an indemnity clause or lowered the sale price). The 7th Circuit of Appeals held that the successor employer in the asset sale can be liable for unpaid pension contributions and delinquent withdrawal liability payments even if the seller dissolved in bankruptcy. (Chicago Truck Drivers, Helpers, and Warehouse Workers Union Pension Fund v. Tasemkin, Inc., 1995 US App. LEXIS 15787 - 7th Cir. 6/26/95). Could other ERISA liabilities, such as fiduciary claims, also move to the buyer? In any case, asset buyers should proceed with caution and may want warranties and indemnifications that are used in stock sales.

In Algio v. RCA Global Communications, Inc. and MCI International, Inc., 60 F. 3d 956 (2nd Circuit (7/12/95), GE sold RCAG to MCI which had a less valuable severance plan. Since the RCAG Board, or anyone who possessed the proper authority, never approved in writing the termination of the RCAG Severance plan, the court said the former plan with the better benefits was still in effect. This case suggests we list all plans when such transactions occur and have the appropriate authority to terminate them as appropriate (and so notify employees).

Actuarial Assumptions

What actuarial assumptions should be used? PBGC's interest and mortality assumptions are deemed to be acceptable per 1.414(l)-1(b)(5), but an IRS spokesperson once said that the PBGC retirement (XRA) assumptions were no longer deemed reasonable especially when early retirement subsidies were available. The concern is: (1) What if one uses the XRA assumption and then (2) the company goes under right after the spinoff, in which case many participants retire immediately (with larger subsidies) making the plan underfunded. Another concern is that REA made contingent benefits available if an employee works long

[22] Because of this, the seller got assurances from the buyer (Pitney)that it would not increase benefits until the seller was off the hook.

enough after a spinoff to qualify for it (e.g. an early retirement subsidy) and PBGC XRAs do not handle that situation well. (EG. PBGC's XRA assumption may be age 58 for a participant even though they may get a subsidized 30 and out early retirement benefit at say age 59 or age 55. Assuming 58 would create present values too low if the employee retired as expected at age 59 or age 55). The XRA assumptions are still often used however, and were approved in arbitration between a very large employer and its employees. The "gray book" at the 1994 EA meeting, which was a synopsis of a meeting with the IRS states that PBGC's new Select and Ultimate interest rates, expenses, and 83GAM assumptions would be deemed reasonable by the IRS. Some at the meeting felt the IRS included the PBGC retirement assumptions (XRA's) in that deeming also. One doesn't have to use PBGC assumptions, but you will lose some protection of the deeming reasonable. It may, however, be more accurate to use some other retirement assumption that reflects the plan and the particular company's or industry's economic climate, post-transaction. If a plan calculates its lump sum based on a 5% interest rate, then the actuary should reflect that option to the extent it would be elected.

How much plan assets should be transferred? The answer to this question often depends on who you represent. For example, the buyer's actuary will often use more conservative assumptions than the seller's actuary (in determining the plan assets to be transferred). The seller's actuary could then suggest to the seller to increase the price of selling his or her company (contending that the buyer could terminate the plan and take the surplus). Other participants have a stake in this too. The participants being transferred will agree with the buyer's actuary, whereas the participants who stay will agree with the seller's actuary. If a spun off plan subsequently terminates and doesn't have enough assets, actuaries could be liable as fiduciaries for recommending the transfer of too little money - so be careful!

One of the best pieces of advice in M&A work (merger and acquisitions) is to invite the actuary in at the earliest stages of thinking and to provide them with all the information they need. There is much litigation in this area as several sections of this study note attest.

APPENDIX A
SAMPLE GUARANTEED BENEFIT CALCULATIONS

CALCULATING MONTHLY BENEFIT GUARANTEED BY THE PBGC

Consider the following participant data. For each of the questions which follow, calculate the guaranteed monthly benefit (GMB). Note that each question refers back to the original, changing only what is relevant to the question. All changes in the calculations are asterisked and footnoted (if clarification is needed).

DOPT -- 1/1/83
Participant Age -- exactly 63 on DOPT
Age of Spouse -- Same as Participant
Benefit Commenced at exactly age 62 = $2000
Form -- J&50%S (contingent)

Benefit under original plan -- $900 (1/1/75)
Benefit under amendment -- $2000 (1/1/82)
Benefit payable at the Normal Retirement Age -- $2,869

(1) What will the participant's guaranteed benefit be?
(2) What if the benefit change on 1/1/82 went to $950?
(3) What if benefit change on 1/1/82 went to $915?
(4) What if monthly earned income was $700/month before retirement?
(5) What if the amendment was effective and adopted 1/2/82?
(6) What if the amendment was effective and adopted 1/1/81?
(7) What if the amendment was adopted 5/1/82 and effective 1/1/82?
(8) What if the amendment were adopted and effective 7/5/79?
(9) What if the plan inception was effective 7/5/79?
(10) What if there was an additional amendment on 11/1/81 which increased benefit from $900 to $1000?
(11) What if their was an amendment adopted 7/5/79, effective 1/1/80 with the following benefit changes:
on 1/1/80, $900 to $1000
on 1/1/81, $1000 to $1200 ?
(12) What if the amendment in (11) were adopted 7/5/80 with the same provisions?
(13) What if DOPT was 1/1/84 (Assume age at DOPT is still 63)?
(14) What if the participant's age on DOPT was 54 1/2 (Assume that the spouse is still the same age as the participant)?

(15) What if age at DOPT was 67 (Assume that the spouse is still the same age as the participant)?
(16) What if benefit did not commence until age 65 (i.e. after DOPT)?
(17) What if the old plan benefit was 5 year certain and continuous, but the new plan is Life Only?
(18) What if old plan benefit was 5 year certain and continuous, but the new plan is 10C&C? (Assume old plan did not have a 10C&C option or factors.)
(19) What if under the old plan the benefit of $900 was payable at the earliest retirement age of 64, while the new plan still allows the benefit of $2000 at age 62?
(20) What if the spouse is age 61 at DOPT (i.e. not the same age as the participant)?
(21) What if the spouse was age 67 at DOPT?
(22) What if the benefit was J&50%S with 7C on benefit commencement date (BCD)?
(23) What if benefit form was 7C&C on benefit commencement date?
(24) What if the benefit form was J&60%S (contingent)?
(25) What if the benefit is 7 years certain?
(26) What if the participant is a substantial owner (s/o)?
(27) What if the participant has been a substantial owner for the last 5 and 1/2 years only?
(28) What if there was a benefit decrease on 1/1/79 to $800 and another decrease on 1/1/82 to $850?
(29) What if the plan had purchased an annuity of $500 for the participant when he retired?
(30) What if the purchased annuity was $1000?
(31) What if the retiree is re-employed and the pension plan allows continuation of benefits upon re-employment?
(32) What if an additional supplement was given from age 62 to age 65 of $900 per month? What else do you need to know? Assume ERF = 6% per year from 65.

(1) What will the participant's guaranteed benefit be?

Maximum Insurance Amount B

$1517.05	(Maximum for 1983)
x .90	(J&50%S factor)
1365.35	
x .86	*(factor for age 63)
$1174.20	(MIA)

* Please note that age 63 (the later of age at Benefit Commencement Date or the age of DOPT, but never over 65) is used for determining the Maximum Insurance Limit, since that is the age at which the PBGC is responsible for making payments.

Date	Years in Effect	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900	900	900	----	100%	900
1/1/82	1	2000	2000	1174.20	274.20	**20%	54.84
							$954.84

** If an amendment has been in effect or adopted less than 5 years prior to DOPT, any increase must be phased in 20% per year (i.e. 4 years prior to DOPT, phase-in = 80%; 3 years prior to DOPT, phase-in = 60%; and so on.

(2) What if the benefit change on 1/1/82 went to $950?

Maximum Insurance Amount

$1517.05	(Maximum for 1983)
x .90	(J&50%S factor)
1365.35	
x .86	(factor for age 63)
$1174.20	(MIA)

Date	Years in Effect	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900	900	900	----	100%	900
1/1/82	1	950	950	950	50	20%	20.00*
							$920.00

* Phased-in amount is the greater of $20 or 20% of $50.

(3) What if benefit change on 1/1/82 went to $915?

Maximum Insurance Amount --	$1517.05	(Maximum for 1983)
x .90	(J&50%S factor)	
$1365.35		
x .86	(factor for age 63)	
$1174.20	(MIA)	

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900	900	900	----	100%	900
1/1/82	1	915	915	915	15	20%	15.00*
							$915.00

* Phased-in amount cannot be greater than the increase.

(4) What if monthly earned income was $700/month before retirement?

Maximum Insurance Amount --	$700.00	*(Maximum for 1983)
x .90	(J&50%S factor)	
630.00		
x .86	(factor for age 63)	
$541.80		

* Maximum for the year is the lessor of the PBGC maximum for that year and 100% of average monthly compensation calculated over the highest five consecutive years of compensation with the employer.

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900	900	541.80	----	100%	541.80
1/1/82	1	2000	2000	541.80	0	20%	0.00
							$541.80

(5) What if amendment was effective and adopted 1/2/82?

Maximum Insurance Amount --	$1517.05	(Maximum for 1983)
x .90	(J&50%S factor)	
1365.35		
x .86	(factor for age 63)	
$1174.20		

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900	900	900	----	100%	900.00
1/2/82	0**	2000	2000	1174.20	1174.20	0%	0.00
							$900.00

** Amendment has not been in effect for one year or more; therefore, there will be no phase-in for the increase. Benefit will be original plan benefit ($900). Note that this is only applicable for pre-SEPPA cases. In post-SEPPA cases, 1/1/86 to 12/31/86 is considered to be one year for phase-in purposes. SEPPA was effective 1/1/86.

(6) What if amendment was effective and adopted 1/1/81?

Maximum Insurance Amount --	$1517.05	(Maximum for 1983)
x .90	(J&50%S factor)	
1365.35		
x .86	(factor for age 63)	
$1174.20	(MIA)	

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900	900	900	----	100%	900.00
1/1/81	*2	2000	2000	1174.20	274.20	40%	109.68
							$1009.68

(7) What if the amendment was adopted 5/1/82 and effective 1/1/82?

Maximum Insurance Amount

$1517.05	(Maximum for 1983)
x .90	(J&50%S factor)
1365.35	
x .86	(factor for age 63)
$1174.20	

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900	900	900	----	100%	900.00
5/1/82	0**	2000	2000	1174.20	0	0%	0.00
							$900.00

** There will be no phase-in. For phase-in purposes, the effective date is considered to be the later of the effective date of the amendment and the adopted date. In this case, even though the amendment was effective 1/1/82, it was adopted 5/1/82 which is less than one year prior to DOPT. There will be no phase-in of the increase, and the benefit will be the original plan benefit ($900).

(8) What if the amendment were adopted and effective 7/5/79?

Maximum Insurance Amount --	$1517.05	(Maximum for 1983)
x .90	(J&50%S factor)	
1365.35		
x .86	(factor for age 63)	
$1174.20	(MIA)	

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900	900	900	----	100%	900.00
7/5/79	*3	2000	2000	1174.20	274.20	60%	164.52
							$1064.52

* Whole years from DOPT

(9) What if the plan inception was effective 7/5/79?

Maximum Insurance Amount -- $1517.05 (Maximum for 1983)
x .90 (J&50%S factor)
1365.35
x .86 (factor for age 63)
$1174.20 (MIA)

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
7/5/79 *3		900	900	900	900	60%	540.00
1/1/82 1		2000	2000	1174.20	274.20	20%	54.84
							$ 594.84

(10)What if there was an additional amendment on 11/1/81 which increased benefit from $900 to $1000?

Maximum Insurance Amount -- $1517.05 (Maximum for 1983)
x .90 (J&50%S factor)
1365.35
x .86 (factor for age 63)
$1174.20 (MIA)

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75 >5		900	900	900	----	100%	900.00
1/1/82 1*		2000	2000	1174.20	274.20	20%	54.84
							$ 954.84

* Whenever there are two or more amendments in any one year period, they are phased-in together using the later plan provisions.

(11) What if there was an amendment adopted 7/5/79, effective 1/1/80 with the following benefit changes: on 1/1/80, $900 to $1000 on 1/1/81, $1000 to $1200?

Maximum Insurance Amount -- $1517.05 (Maximum for 1983)
x .90 (J&50%S factor)
1365.35
x .86 (factor for age 63)
$1174.20 (MIA)

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900	900	900	----	100%	900.00
1/1/80	3	1000	1000	1000	100	60%	60.00
1/1/81	*2	1200	1200	1174.20	174.20	40%	69.68
1/1/82	1	2000	2000	1174.20	0	20%	0.00
							$1029.68

* Whenever an amendment makes changes which are effective on dates specified in the amendment, the effective date is considered to be the later of the effective date of the amendment, the adopted date of the amendment, and the effective date of provision as specified in the plan. Each provision is, therefore, considered separately.

(12) What if the amendment in (11) were adopted 7/5/80 with the same provisions?

Maximum Insurance Amount -- $1517.05 (Maximum for 1983)
x .90 (J&50%S factor)
1365.35
x .86 (factor for age 63)
$1174.20 (MIA)

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900	900	900	----	100%	900.00
1/1/81	*2	1200	1200	1174.20	274.20	40%	109.68
1/1/82	1	2000	2000	1174.20	0	20%	0.00
							$1009.68

* The date for phase-in purposes for the first change is its adopted date (7/5/80) and, for the second change, it is its effective date (1/1/81); therefore, both changes have been in effective for 2 whole years prior to DOPT. Thus they are phased-in together.

(13) What if DOPT was 1/1/84 (Assume age at DOPT and BCD are still 63 and 62)?

Maximum Insurance Amount --	$1602.27	(Maximum for 1984)*
x .90	(J&50%S factor)	
1442.04		
x .86	(factor for age 63)	
$1240.15	(MIA)	

* When calculating the MIA, be sure to use the maximum set in the year of DOPT (no matter whether the participant is retired on DOPT or not).

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900	900	900	----	100%	900.00
1/1/82	2	2000	2000	1240.15	340.15	40%	136.06
							$1036.06

(14) What if the participant's age on DOPT was 54 1/2? (Assume spouse is still the same age as participant)

Maximum Insurance Amount --	$1517.05	(Maximum for 1983)
x .90	(J&50%S factor)	
1365.35		
x .44	*(factor for age 54 1/2)	
$600.75	(MIA)	

* When calculating MIA, be sure to use correct factor for age at DOPT.

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900	900	600.75	----	100%	600.75
1/1/82	1	2000	2000	600.75	0	20%	0.00
							$ 600.00

(15) What if age at DOPT was 67? (Assume spouse is still same age as participant)

Maximum Insurance Amount --	$1517.05	(Maximum for 1983)
x .90	(J&50%S factor)	
1365.35		
x 1.00	*(factor for age 67)	
$1365.35	(MIA)	

* Note that there is no increase in the maximum for age over 65.

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900	900	900	----	100%	900
1/1/82	1	2000	2000	1365.35	465.35	20%	93.07
							$ 993.07

(16) What if benefit did not commence until age 65 (i.e. after DOPT)?

Maximum Insurance Amount --	$1517.05	(Maximum for 1983)
x .90	(J&50%S factor)	
1365.35		
x 1.00	**(factor for age 65)	
$1365.35	(MIA)	

** Factors used to calculate MIA depend on age at DOPT or benefit commencement, whichever is later. Also note that the factor for age 65 and over is 1.00.

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900	900	900	----	100%	900
1/1/82	1	2000	2000	1365.35	465.35	20%	93.07
							$ 993.07

(17) What if the old plan benefit was 5 year certain and continuous, but the new plan is Life Only?

Before phase-in, you must normalize the benefits (i.e. put them in the same form as the final benefit). When normalizing, use the plan document for factors. If there are no such factors in the plan document, use PBGC's factors. Say the plan gives a conversion factor of 1.04.

Maximum Insurance Amount	
$1517.05	(Maximum for 1983)
x 1.00*	(Life Only factor)
1517.05	
x .86	(factor for age 63)
$1304.66	(MIA)

* Note that the final form is Life Only.

Date	Years in Effect	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900 (5C&C)	936** (LO)	936	----	100%	936
1/1/82	1	2000	2000 (L.O.)	1304.66	368.66	20%	73.73
							$1009.73

** Convert 900, which is 5C&C, to Life Only using plan conversion factor of 1.04.

(17a) If the plan did not have conversion factors, then it is necessary to use PBGC's factors as follows:

Maximum Insurance Amount remains unchanged.

Years in Date Effect		Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900	*923.08	923.08	----	100%	936
1/1/82	1	2000	2000	1304.66	381.58	20%	76.32
							$ 999.40

* When normalizing using PBGC factors (found in maximum benefit section 4022.23), multiply the benefit by the following ratio of factors:

(Type of new form)(Age when benefit starts)(Age Difference)
(Type of old form)(Age when benefit starts)(Age Difference)

In this situation, the benefit ($900) would be multiplied by

(1.0)(0.79)(1.0)
(0.975)(0.79)(1.0) = 1.02564

(18) What if old plan benefit was 5 year certain and continuous, but the new plan is 10C&C? (Assume old plan did not have a 10C&C option or factors.)

Maximum Insurance Amount --	$1517.05	(Maximum for 1983)
x 0.935*	(9C&C factor)	
1418.44		
x .86	(factor for age 63)	
$1219.86	(MIA)	

* Use certain period left at DOPT

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900 (5C&C)	*853.35 (10C&C)	*853.85	----	100%	835.85
1/1/82	1	2000 (10C&C)	2000 (10C&C)	1219.86	366.01	20%	73.20
							$ 927.05

(19) What if under the old plan the benefit of $900 was payable at the earliest retirement age of 64, while the new plan still allows the benefit of $2000 at age 62?

Maximum Insurance Amount --	$1517.05	(Maximum for 1983)
x 0.90	(J&50%S factor)	
1365.35		
x .86	(factor for age 63)	
$1174.20	(MIA)	

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900 @64	*764.52	764.52	----	100%	764.52
1/1/82	1	2000 @62	2000	1174.20	409.68	20%	81.94
							$ 846.46

* Using PBGC factors, the normalized benefit at 62 would be 900 * (.79/.93) = 764.52. Note that one first reduces benefit at Normal Retirement Age down to the earliest Early Retirement Age in the old plan (age 64) using the old plan factors. Then the reduction is extended to age 62 using PBGC factors.

(20) What if the spouse is age 61 at DOPT (i.e. not the same age as the participant)?

Maximum Insurance Amount --	$1517.05	(Maximum for 1983)
x 0.90	(J&50%S factor)	
1365.35		
x .86	(factor for age 63)	
$1174.20		
x 0.98	*	(factor for two year (MIA)
$1150.72	*	younger age difference)

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900	900	900	----	100%	764.52
1/1/82	1	2000	2000	1150.72	250.72	20%	50.14
							$ 950.14

(21) What if the spouse was age 67 at DOPT?

Maximum Insurance Amount --	$1517.05	(Maximum for 1983)
x 0.90		(J&50%S factor)
1365.35		
x .86		(factor for age 63)
$1174.20		
x 1.01	*	factor for two years (MIA)
$1185.94		older age difference)

* Factor for age differences: use 65 for employees and/or spouses if over 65.

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900	900	900	----	100%	900.00
1/1/82	1	2000	2000	1185.94	285.94	20%	57.19
							$ 957.19

(22) What if the benefit was J&50%S with 7C on benefit commencement date (BCD)?

Maximum Insurance Amount --	$1517.05	(Maximum for 1983)
x 0.90		(J&50%S factor)
1365.35		
x .976	*	(w/ 6C factor)
$1332.58		
x .86		(factor for age 63)
$1146.02		(MIA)

* When form is J&S with m years certain, adjust the insurance limit for age and J&S form , and then adjust for the m years left of the C&C as of DOPT. To find the factor, you must interpolate using the following numbers -- at m = 10, the factor is 0.96, and at m = 0, the factor is 1.

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900	900	900	----	100%	900.00
1/1/82	1	2000	2000	1146.02	246.02	20%	49.20
							$ 949.20

(23) What if benefit form was 7C&C on benefit commencement date?

Maximum Insurance Amount --	$1517.05	(Maximum for 1983)
x .965	*	(6C&C factor)
1463.95		
x .86		(factor for age 63)
$1259.00		(MIA)

* Convert to years certain as of DOPT.

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900	900	900	----	100%	900.00
1/1/82	1	2000	2000	1259	359	20%	71.80
							$ 971.80

(24) What if benefit form was J&60%S (contingent)?

Maximum Insurance Amount --	$1517.05	(Maximum for 1983)
x 0.88	*	(J&60%S factor)
1335.00		
x .86		(factor for age 63)
$1148.10		(MIA)

* To find the J&60%S factor, you must interpolate between PBGC's given factors. In this case, the factor for J&50%S is 0.90 and the factor for J&100%S is 0.80. Therefore, by interpolation, the J&60%S factor is 0.88.

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900	900	900	----	100%	900.00
1/1/82	1	2000	2000	1148.10	248.10	20%	49.62
							$ 949.62

(25) What if benefit is 7 years certain on DOPT?

Maximum Insurance Amount --	$1517.05	(Maximum for 1983)
x .86		(factor for age 63)
1304.66		
x 1.479		**(factor for 7 C)
$1929.59		(MIA)

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900	900	900	----	100%	900.00
1/1/82	1	2000	2000	1929.59	1029.59	20%	205.92
							$1105.92

** To adjust the maximum benefit for annuity certain, use the following method:
Let Y be the later of age nearest birthday and age at Benefit Commencement Date.

Insurance limit times Present Value of SLA at age Y-1(Male)
at Y Present Value of Annuity certain period

In this case, the maximum was adjusted using the factor
7.5849 which resulted in the factor of 1.479.
5.1283

(26) What if the participant is a substantial owner (s/o)? Assume she/he had 7 years of service

Maximum Insurance Amount --	$1517.05	(Maximum for 1983)
x 0.90		(J&50%S factor)
1365.35		
x .86		(factor for age 63)
$1174.20		(MIA)

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	8	900	900	900	----	7/30	210.00
1/1/82	1	2000	2000	1174.20	274.20	1/30	9.14
							$ 219.14

* If the participant is a substantial owner, the phase-in is over 30 years instead of the 5 years for non-substantial owners. Therefore, each is phased in 1/30th (i.e. multiply by the number years in effect during which the s/o was an active participant in plan divided by 30).

(27) What if the participant has been a substantial owner for his last 5 and 1/2 years only?

In this case, the participant is considered a partial substantial owner and his benefit is calculated as follows:

Benefit if participant had always been s/o = 219.14(see #26).
Benefit if participant had never been s/o = 954.84 (see #1).
Participant was an active s/o 5.5 of the 7 years.
Participant was not an active s/o 1.5 of the 7 years.

The participant's guaranteed benefit will be calculated by prorating the above benefits.

GMB = 219.14 * (5.5/7) + 954.84 (1.5/7)
= 376.79

(28) What if there were decreases in the benefit formula such that the DOPT accrued benefit under the 1/1/79 plan was $800 and under the 1/1/82 plan it became $850?*

* Actually, while an employee's prospective benefit can decrease, it is not legal to decrease an employee's accrued benefit. A plan document would have to ensure that the accrued benefit did not decrease. Assume here that the accrued benefit did not decrease.

Maximum Insurance Amount --	$1517.05	(Maximum for 1983)
x 0.90		(J&50%S factor)
1365.35		
x .86		(factor for age 63)
$1174.20		(MIA)

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	5	900	800*	800	----	100%	800
1/1/79	4	800	800	800	0	----	----
1/1/82	1	850	850	850	50	20%	20
							$820

THE GUARANTEED MONTHLY BENEFIT IN THIS CASE IS $820.

* Ignore the fact that the benefit projected to DOPT in the original plan was even greater than the $800 benefit in the 4 year old plan.

(29) What if the plan had purchased an annuity of $500 for the participant when he retired?

Maximum Insurance Amount --	$1517.05	(Maximum for 1983)
x 0.90		(J&50%S factor)
1365.35		
x .86		(factor for age 63)
$1174.20		(MIA)

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900	900	900	-----	100%	900
1/1/82	1	2000	2000	1174.20	274.20	20%	54.84
							$954.84
							-500.00
							$454.84

Whenever an annuity is purchased prior to DOPT for a portion of the plan benefit, the PBGC guaranteed benefit will be calculated as follows: First, calculate the entire phased-in guaranteed benefit. Second, subtract the purchased annuity from the phased-in guaranteed benefit.

Please note that for deferred participants the amount subtracted should be based on the actual annuity paid (i.e., Use current annuity purchase rates if that is what eventually will be used to determine the annuity at BCD. Use guaranteed annuity purchase rates if the insurance company only will pay using the guaranteed rates.)

(30) What if the purchased annuity was $1000?

Since the participant's calculated guaranteed benefit is less than the annuity purchased, PBGC will not guarantee any benefit for this participant.

(31) What if the retiree is re-employed and the pension plan allows continuation of benefits upon re-employment?

This benefit will be suspended by PBGC until re-retirement.

(32) What if an additional supplement was given from age 62 to age 65 of $900 per month? What else do you need to know? Assume ERF = 6% per year from 65.

Maximum Insurance Amount --	$1517.05	(Maximum for 1983)
x 0.90		(J&50%S factor)
1365.35		
x .86		(factor for age 63)
$1174.20		(MIA)

Years in Effect	Date	Benefit	Normalize	Limited to Max	Increase	P/I	P/I Amount
1/1/75	>5	900	900	900	----	100%	900
1/1/82	1	*2869 (up to 65) 2000 (after 65)	**2146.86	1174.20	274.20	20%	54.84
							***$954.84

* The actual benefit here is 2000 + 900 = 2900, but the PBGC will only guarantee up to the accrued benefit at normal retirement. Let's assume that the accrued benefit at normal retirement is $2869.

** The $2869/$2000 benefits were levelized. To do this, the following steps must be followed:

a. Determine the amount of temporary supplemental income which exceeds the level life annuity (i.e. 2869 - 2000 = 869).

b. Apply the appropriate level life factor-tables in 29 CFR 4022.23(f)-to amount in (a) based on age at DOPT (to years and next higher month) and age at which temporary supplement stops. (In this case, age at DOPT is 63 yrs. 0 months and the supplement ends at age 65. The factor is, therefore, 0.169. After applying the factor on (a), the result is 146.86)

c. Add amount determined in (b) to level life annuity and compare to maximum guaranteed limit (i.e. 2000 + 146.86 = 2146.86).

*** Now that the levelized guaranteed amount has been determined, it must be converted back to step-down form with the same ratio of temporary to life annuity as in the original step-down annuity.

954.84 times 2869 = $1279.02 up to age 65
2146.86

954.84 times 2000 = $889.53 after 65
2146.86

Note that because this benefit was over the maximum, the employee gets the same present value as the employee in Q&A#1, except the form is as a step-down annuity instead of level life.

Guaranteeable Benefits Quiz

(1) Name 6 reasons why the PBGC will not guarantee a benefit.

1. Not nonforfeitable
2. Not entitled
3. Not pension benefit
4. It is greater than the accrued at normal
5. Phase/In
6. Over max

(2) On the benefits listed on the next page, please determine:

1. Are they guaranteeable (basic-type)?
2. Are they guaranteed (basic)?
3. If not guaranteed, give reason (see Q&A #1)?
4. Are they in PC5 (benefit commitments)?
5. Are they in PC6 (benefit liabilities)?
6. Are the protected by 411(d)(6) = anti-cutback rule?

(continued on next page)

BENEFIT	1. Guaranteeable?	2. Guaranteed ?	3. Why?	4. PC5?	5. PC6?	6. Protected?
Gold Watch	N	N	Not Pension Benefit	Y ?	Y ?	N
Lump Sum	N	N	Not Pension Benefit	Y	Y	Y
$1,000/mo. benefit for life @65	Y	Y	-	-	-	Y
$5,000/mo. benefit for life @65	Y	N	>Max	Y	-	Y
Benefits to non-vested: - active employee - separated employee	 N N	 N N	 Not non-forfeit Not non-forfeit	 N N	 Y Depends	 Y Depends
Non-vested portion to an - active employee - separated employee	 N N	 N N	 Not non-forfeit Not non-forfeit	 N N	 Y Depends	 Y Depends
Supplement (on top of an unreduced accrued ERB)	N	N	acc @ NRA	Y if elig	Y from future svc	N
Disability benefit if ee is in 6 month waiting period on DOPT	Y	Y	-	-	-	N
Return on mandatory EEC on death	Y	Y	-	-	-	Y
Future disability benefit	N	N	Not non-forfeit	N	Y	N
Future death benefit of $1	N	N	Not non-forfeit	N	Y	N
Benefits after re-employed	N	N	Not pension b	N	N	N
20 c&c optional form for a deferred; not elected on DOPT	N	N	Not entitled	Y	Y	Y
20 c&c optional form for already retired	Y	Y	-	-	-	Y
SSLO for someone already retired	Y	Y	-	-	-	Y
SSLO for worker not retired & not elected	N	N	Not entitled	Y	Y if not vested	Y
Disability ben in pay status > acc@NRA	Y	Y	-	-	-	N
55&30 subsidized early benefit - for someone @ 54&29 - for someone @ 55&29 - for someone @ 54&30 - for someone @ 56&31	 N N N Y	 N N N Y	 not non-forfeit " " -	 N N N -	 Y from future svc " " 	 Y Y Y Y
Pre Retirement Survivor Annuity (PBGC version)	Y	Y	-	Y by 4022(e)	-	N
automatic COLAs	N	N	not subject to P/I	Y	Y if not vested	Y
future accruals	N	N	not entitled non-forfeit	N	N	N
shutdown benefits - supplements - shutdown in past - shutdown in future	up to Acc@NRA N	up to Acc@NRA N	acc@NRA Not non-forfeit	 Y N	 - Y	 N N
shutdown benefits - subsidized ERRF - past shutdown - future shutdown	 Y N	 Y N	 - Not non-forfeit	 Y N	 - Y	 Y N

APPENDIX B

Joint Implementation Guidelines

IRS General Information Response on Deductibility

DOL Fiduciary Letters
DOL Advisory Opinion on Expenses (Settlor Functions discussed)
DOL Letter On Fiduciary Responsibility And Plan Terminations

STANDARD TERMINATION AUDIT LETTER
SAMPLE PREMIUM AUDIT LETTER FROM PBGC
SAMPLE PARTICIPANT NOTICE AUDIT LETTER FROM PBGC

JOINT IMPLEMENTATION GUIDELINES

PBGC News Release 84-23 (Retype)

Joint Implementation Guidelines on Asset Reversions issued by ERISA Agencies.

The Pension Benefit Guaranty Corporation (PBGC) announced today that along with the Treasury Department and the Department of Labor, it has agreed to joint implementation guidelines for dealing with pension plan terminations in which the employer recovers excess assets. The agencies are now proceeding to process cases in accordance with these guidelines. Appropriate steps will be taken by each agency through regulations and otherwise to establish the indicated procedures.

"We believe that the implementation guidelines we are adopting reflect a fair balancing of the rights of plan participants, plan sponsors, and the public interest," said Charles Tharp, executive director of the PBGC. "It is important that plan participants receive the full benefits to which they are entitled at termination, while recognizing the rights of plan sponsors to any surplus above that. And we believe it is essential that policies in this area encourage the establishment and maintenance of defined benefit pension plans."

Implementation Guidelines

The following has been adopted by the Department of the Treasury, the Department of Labor and the Pension Benefit Guaranty Corporation to provide guidelines for processing defined benefit pension plan terminations involving asset reversions to the plan sponsor.

1. In accordance with current law, when an employer terminates a defined benefit pension plan, it may not recover any surplus assets until it has fully vested all participants' benefits and has purchased and distributed annuity contracts, to protect participants against the risk that their accrued benefits may be jeopardized by future market fluctuations or other factors.

2. At present, upon plan termination, employers can make lump sum payments to certain participants. In some cases, these lump sums have been calculated on the basis of interest rates that are higher than those available to individuals, thereby reducing the value of those benefits. This problem must be addressed. If employees are offered lump sum payments in lieu of future pensions, the amount of the lump sum must fairly reflect the value of the pension to the individual. The Pension Benefit Guaranty Corporation is developing guidelines for determining appropriate lump sum values.

3. An employer that terminates a sufficient defined benefit pension plan may establish a new defined benefit plan covering the same group of employees. The new plan may grant past service credit for the period during which an employee was covered by the terminated plan (subject to the limitations of Section 415 of the Internal Revenue Code). The prior plan and the new plan, in combination, may provide benefits for each participant equivalent to those to which the participant would have been entitled if the prior plan had continued without interruption. The PBGC will clarify the fact that a successor plan is exempt from the five year phase-in of benefit guarantees that applies to newly established plans. The above is one example of what will be deemed a successor plan by the PBGC.

4. In the case of a so-called "spin-off/termination", generally no termination will be recognized and any attempt to recover surplus assets will be treated as a diversion of assets for a purpose other than the exclusive benefit of employees and beneficiaries unless the following conditions are satisfied:

* The benefits of all employees (including those covered by the ongoing plan) must be fully vested and non-forfeitable as of the date of termination.

* All benefits accrued as of the date of termination in the ongoing plan must be provided for by the purchase of annuity contracts which represent irrevocable commitments for the benefit of each individual participant.

* All employees who were covered by the original plan must be given advance notice of the transaction in similar time and manner as if the entire original plan were being terminated.

5. In the case of a so-called "spin-off/termination" and a so-called "termination/re-establishment" transaction, generally any attempt to recover surplus assets will be treated as a diversion of assets for a purpose other than the exclusive benefit of employees and beneficiaries unless the following conditions are satisfied:

(a) In the case of an ongoing plan described in number 4 above, the funding method for the ongoing plan must be changed on the date of termination by combining and offsetting amortization bases in accordance with §412(b)(4) of the Code. The amortization period for this base will be the lesser of the combined amortization period and the weighted average future remaining working lifetime of all covered employees. The employer must request and obtain IRS approval for this change in funding method.

(b) In the case of a new plan established with credit for past service as described in number 3 above, in order to obtain a reversion of surplus assets from the terminated plan, the future amortization period for the unfunded past service liability for the new plan, under Section 412 of the Code, will be the lesser of 30 years and the weighted average future remaining working lifetime of all covered employees. The employer must request and obtain IRS approval for this change in funding method for the new plan.

The agencies' analysis indicates that, in spinoff/terminations where the conditions in numbers 4 and 5a are satisfied, the security of participants' benefits is protected by the purchase and distribution of annuities, the statutory minimum funding rules, including the rules described in number 5(a), and PBGC insurance coverage.

6. Employers are reminded that one of the requirements for plan qualification is that the plan be intended to be permanent. In any case, the funding rules generally require that plan funding be on a going-concern basis rather than on a termination basis. Thus, the tax consequences of multiple "termination/reestablishment" or "spinoff/terminations" are unaffected by these guidelines and will be determined without regard to whether the specific guidelines described above are satisfied with regard to each of the transactions. Generally, an employer may not engage in either a termination/reestablishment or spin-off/termination transaction, involving reversion of assets, any earlier than 15 years following any such transaction.

7. The federal income tax consequences of the receipt of reversions, of deductions for contributions to ongoing or successor plans and of the funding of such plans, after the change in funding method, are unaffected by these guidelines.

8. The PBGC will continue to process and the IRS will now proceed to process all pending termination cases.

IRS GENERAL INFORMATION RESPONSE ON DEDUCTIBILITY

Mr. C. Frederick Reish
Reish & Luftman
11755 Wilshire Boulevard
10th Floor
Los Angeles, CA 90025

Dear Mr. Reish:

This in response to your general information request of May 31, 1990 in which you requested guidance as to when a plan must distribute assets upon termination.

Rev. Rul. 89-87, 1989-2 C.B. 81, provides that in order for a plan to terminate it must distribute all plan assets as soon as administratively feasible. In general, whether assets are distributed as soon as administratively feasible is based on the facts and circumstances of a given case. Rev. Rul 89-87 provides that, in general, any distribution that is completed more than one year after the intended date of termination will be presumed not to be administratively feasible. Thus, a plan sponsor will generally bear a heavier burden of proof in showing that a distribution of plan assets was completed as soon as administratively feasible if such distribution is completed more than one year after the intended date of termination.

Since the determination as to whether a distribution is completed as soon as administratively feasible is based on the facts and circumstances of the given case, we cannot, in a general information letter, address whether the specific facts in your case constitute an administratively feasible distribution. There are however, certain circumstances which will generally be considered proper reasons to delay the distribution of plan assets. For example, if a plan sponsor submits a timely application for a determination letter upon termination, the plan sponsor may delay the distribution of assets until the determination letter is issued. In addition, if circumstances exist which are outside of the control of the plan fiduciaries that prevent the distribution of plan assets, it may be administratively feasible to delay the distribution of plan assets beyond the one-year period set forth in Rev. Rul. 89-87. However, a plan sponsor does not meet the burden of showing that plan assets were distributed as soon as administratively feasible merely because such distribution was delayed on account of an audit of the employer by the Internal Revenue Service.

You also requested information concerning the applicability of the nondeductible contribution penalty tax under section 4972 of the Code. In general, section 4972 provides a 10% penalty tax on contributions made during a year to the extent they are not deductible under section 404 of the Code. In addition, the penalty tax under section 4972 continues to apply until such time as the excess amount is corrected. However, upon plan termination the penalty tax under section 4972 no longer applies since there is no longer a "qualified employer plan," as defined under section 4972(d)(1), upon which to apply the section 4972 penalty tax. Thus, the penalty tax will only be applied for years prior to the date of plan termination.

We hope the above general information is helpful to you. Please note, however, this is not a ruling and may not be relied on as such.

Sincerely yours,

Ken Yednock
Chief, Employee Plans
Projects Branch

RETYPE OF DOL ADVISORY OPINION ON EXPENSES (SETTLOR FUNCTIONS DISCUSSED)

March 2, 1987

Mr. Kirk F. Maldonado
Stradling, Yocca, Carlson & Rauth
660 Newport Center Dr., Suite 1600
Newport Beach, CA 92660-6441

Dear Mr. Maldonado:

This is in response to your letter of July 16, 1986, and subsequent letters of August 26, 1986, and October 14, 1986, in which you request an advisory opinion on the application of the Employee Retirement Income Security Act (ERISA) to the payment of certain expenses by the Canoga Park Hospital Retirement Plan (the Plan).

You represent that the Plan specifies that it may pay certain administrative expenses incurred in the operation of the Plan which are explicitly set forth to include:

(1) Attorney's fee incurred in connection with amending the plan to comply with legislative, case law and regulatory developments;

(2) Annual valuations of the sponsoring employer's stock held by the Plan;

(3) Annual audit of the Plan performed by a certified public accountant;

(4) The fees of an outside consultant performed in connection with the administration of the Plan (e.g., preparation of benefit statements to participants); and

(5) The fees paid to members of the Committee. (Subject to the rule of ERISA section 408(c)(2), prohibiting payment of compensation by a plan to any individual who is receiving full-time pay from an employer whose employees are participants in the plan.)

You ask whether the above expenses authorized by the plan constitute "expenses of administering the plan" within the meaning of sections 403(c)(1), and 404(a)(1)(A) of ERISA. You further ask whether the expenses incurred in connection with the bonding requirements of section 412 of ERISA could be charged to the plan.

Your inquiry relating to whether or not the payment by the Plan of the expenses described in your letter would be an appropriate expenditure of plan assets involves factual considerations with respect to which the Department will ordinarily not provide an opinion. (See section 5.04 of ERISA Procedure 76-1, 41 FR 36281, August 27, 1986.) Therefore, the following discussion is intended to provide general guidance with respect to the various legal issues raised by your questions.

In evaluating the propriety of the payment of plan assets for certain expenses, plan fiduciaries must first consider the general fiduciary responsibility provisions of sections 403 and 404 of ERISA. Section 403(c)(1) of ERISA provides, in relevant part, that the assets of an employee benefit plan shall never inure to the benefit of any employer and shall be held for the exclusive purpose of providing benefits to participants and beneficiaries and defraying reasonable expenses of administering the plan. Similarly, section 404(a)(1)(A) of ERISA requires, in pertinent part, that a fiduciary of a plan discharge his duties for the exclusive purpose of providing benefits to participants and beneficiaries and defraying reasonable expenses of administering the plan. Thus, a payment that is not a distribution of benefits to participants or beneficiaries of a plan would not be consistent with the requirements of sections 403(c)(1) and 404(a)(1)(A) of ERISA unless it were used to defray a reasonable expense of a reasonable expense of administering the plan. For example, the use of plan assets to pay fees and expenses incurred in connection with the provision of services would not be a reasonable expense of administering a plan if the payments are made for the employer's benefit or involve services for which an employer could reasonably be expected to bear the cost in the normal course of such employer's business or operations. In this regard, certain services provided in conjunction with the establishment, termination and design of plans, so called "settlor" functions, relate to the business activities of an employer and, therefore, generally would not be the proper subject of payment by an employee benefit plan. It is the responsibility of appropriate plan fiduciaries to determine whether a particular expense is a reasonable administrative expense under sections 403(c)(1) and 404(a)(1)(A) of ERISA.

The prohibited transaction provisions also come into play in connection with payments for administrative services. Section 406(a)(1)(C) and (D) of ERISA provide, in part, that a fiduciary with respect to an employee benefit plan shall not cause the plan to engage in a transaction if he or she knows or should know that such transaction constitutes a direct or indirect furnishing of goods, services or facilities between the plan and a party in interest with respect to the plan or transfer to, or use by or for the benefit of, a party in interest of any assets of the plan.

Subject to the limitations of section 408(a) of ERISA, section 408(b)(2) exempts from the prohibitions of section 406(a) any contract or reasonable arrangement with a party in interest, including a fiduciary, for office space, or legal, accounting or other services necessary for the establishment or operation of a plan, if no more than reasonable compensation is paid therefor. Regulations issued by the Department clarify the terms "necessary service" (29 CFR §2550.408b-2(b), "reasonable contract or arrangement" (29 CFR 2550,408b-2(c)) and "reasonable compensation" (29 CFR 2550.408b-2(d)) as used in section 408(b)(2) of ERISA. What constitutes a "necessary service" in a particular case, however; can only be resolved by taking into account the relevant facts and circumstances. Thus, the fiduciaries of a plan should review all services provided to determine whether such services are "necessary services" for which payment would be lawful.

With regard to your specific question as to the payment of expenses incurred in connection with the bonding requirements of section 412 of ERISA, the Department has stated in its ERISA Interpretive Bulletin, 29 CFR 2509.75-5, at question and answer number FR-9, that the purchase by a plan of a bond covering plan officials, as required by section 412(a) of ERISA will not be deemed a prohibited transactlon under sections 408(a) or (b) of ERISA.

We hope that this information has been helpful to you.

Sincerely,

Elliot I. Daniel
Associate Director for
Regulations and Interpretations

RETYPE OF DOL LETTER ON FIDUCIARY RESPONSIBILITY AND PLAN TERMINATIONS

March 13, 1986

Mr. John N. Erlenborn
Hayfarth, Shaw, Fairweather & Geraldson
111 19th Street, N.W.
Washington, D.C. 20036

Dear Mr. Erienborn:

In you capacity as chairman of the Advisory Council on Employee Welfare and Pension Benefit Plans, you have requested an opinion of the Department of Labor regarding the interplay between the fiduciary responsibility provisions of ERISA and pension plan terminations. Specifically, it appears that several witnesses at the public hearing held by the Advisory Council Task Force on Termination Reversions on January 13, 1986, raised questions regarding the extent to which ERISA's fiduciary duty rules would apply to the decision to terminate a pension plan and activities undertaken pursuant to that decision. You indicated that a Departmental opinion on these issues would be helpful to the Advisory Council Task Force in its current deliberations. Pursuant to your request, we have examined past Departmental pronouncements and court cases relevant to this area. Although it is difficult to provide detailed guidance in an absence of specific factual situations, we believe there are a number of general conclusions which may be helpful to the Advisory Council Task Force.

First, in light of the voluntary nature of the private pension system governed by ERISA, the Department has concluded that there is a class of discretionary activities which relate to the formation, rather than the management of plans. These so-called "settlor" functions include decisions relating to the establishment, termination and design of plans and are not fiduciary activities subject to Title I of ERISA. In Congressional testimony, the Department has consistently taken the position that the decision to terminate a pension plan is such a settlor, or business activity and is therefore not subject to ERISA's requirements. Courts have agreed with the Department's analysis in light of the voluntary nature of the private pension system and ERISA's overall statutory scheme. See, for example, U.A.W. District 63 v. Harper & Row, Inc. 576 Supp. 1468 (S.D.N.Y. 1983), Walsh v. Great Atlantic and Pacific Tea Co., 96 F.R.D. (632 D.N.J. 1983), aff'd T36 F2d (3rd Cir.): Washington-Baltimore Newspaper Guild, Washington Star Co. 655 F. Supp. 257 (D.D.C. 1983).*

Although the decision to terminate is generally not subject to the fiduciary responsibility provision of ERISA, the Department has emphasized that activities undertaken to implement the termination decision are generally fiduciary in nature. As you are aware, fiduciary activities governed by Title I of ERISA are not restricted to activities undertaken by fiduciaries denominated as such. Rather, as a general matter, ERISA establishes a functional approach to determine whether an activity if fiduciary in nature. Section 3(21)(A) of ERISA states:

Except as otherwise provided in subparagraph (E), a person is a fiduciary with respect to a plan to the extent (1) he exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets (ii) he renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so, or (iii) he has any discretionary authority or discretionary responsibility in the administration of such plan. Such term includes any person designed under section 405(c)(1)(B).

Pursuant to this provision, the Department has indicated that it will examine the types of functions performed, or transactions undertaken, on behalf of a plan to determine whether such activities are fiduciary in nature and therefore subject to ERISA's fiduciary responsibility provisions. 29 CFR 2509.75-3, D-2. Although persons holding certain positions with a plan (for example, plan administrator) will be plan fiduciaries because of the discretionary nature of the duties attendant upon such position, fiduciary status is not limited to persons occupying those positions. Rather, it is the function performed that will determine fiduciary status. 39 CFR 2509.75-3, D-3. Thus, for example, the employer or officers or directors of the employer, will be subject to the fiduciary provisions of ERISA to the extent that the employer's functions with regard to the plan are among the types of activities enumerated in ERISA section 3(21)(A). 29 CFR 3509.75-3, D-4.

In light of this functional approach, we have examined a number of examples of activities undertaken pursuant to the decision to terminate. This is not intended to be an exhaustive treatment of all possible scenarios; rather, the purpose of these analyses is to provide guidance as to the factors relevant to each determination.

1. **Determinations under Section 4044(d)(1) of ERISA. S**ection 4044(d) sets forth three conditions which must be met before surplus assets may revert to the plan sponsor upon termination:

Any residual assets of a single employer plan may be distributed to the employer if:
(A) all liabilities of the plan to participants and their beneficiaries have been satisfied.
(B) the distribution does not contravene any provision of law, and
(C) the plan provides for such a distribution in these circumstances.

The first of these conditions - the satisfaction of liabilities is discussed below. The other two criteria involve the interpretation of plan documents to determine if a reversion was allowed and the identification of legal considerations concerning the disposition of plan assets in the form of a reversion. Both of these undertakings involve discretionary authority or discretionary responsibility in the administration of the plan, and as a result, an individual exercising this authority or responsibility would be a fiduciary pursuant to Section 3(21)(A)(iii) of ERISA.

2. **Allocation of Assets under Section 4044(d)(2).** Section 4044 of ERISA requires that the plan administrator allocate assets upon termination to benefit classes in the order prescribed in section 4044(a). As noted above, section 4044(d)(1) describes the circumstances under which a plan sponsor may receive a reversion of surplus assets. Section 4044(d)(2) contains a special rule dealing with surplus assets in the case of a contributory defined benefit plan:

Notwithstanding the provisions of paragraph (1), if any assets of the plan attributable to employee contributions remain after all liabilities of the plan to participants and their beneficiaries have been satisfied, such assets shall be equitably distributed to the employees who made such contributions (or their beneficiaries) in accordance with their rate of contributions.

The process of allocation is carried out by the plan administrator subject to PBGC regulations.

Pursuant to the foregoing discussion of fiduciary activity, it appears that allocation decisions under section 4044, including section 4044(d)(2), are fiduciary decisions. The allocation of assets is among the first steps taken to implement the decision to terminate a plan. Allocation decisions involve the type of disposition of plan assets generally treated as fiduciary activity. Thus, when the plan administrator acts pursuant to section 4044, his activities will also be subject to the fiduciary duty provisions of ERISA.

3. **Choice of Insurer.** Current law requires that, as a general rule, a plan provide for benefits upon termination through the purchase of an annuity. 29 CFR §§2617.4(a), 2617.21. The PBGC does not maintain standards governing the identity, financial status, etc. of insurers issuing annuities to close out plans. Such matters are generally the subject of state insurance regulation. However, where more than one insurer is available to issue an annuity closing out a plan, it is incumbent upon the plan administrator to choose among such insurers. See 29 CFR 2617.21(a) (the duty of purchasing the annuity with plan assets rests with the plan administrator).

Consistent with the functional analysis of fiduciary activities, the choice of an insurer would appear to involve the type discretionary authority over the disposition of plan assets covered in section 3(21)(A). Regulation 29 CFR '2617.21(a) requires that, within ninety days after the date of the Notice of Sufficiency, the plan administrator shall allocate and distribute plan assets by "purchasing from an insurer contracts to provide benefits required ... to be provided in annuity form." Therefore, it appears that the fiduciary provisions of ERISA, including the prudence requirement of section 404(a)(1)(B) will apply to the choice of an insurer to issue annuities upon plan termination.

4. **Lump Sum Interest Rates.** PBGC regulation 29 CFR 2617.4(b) provides that, under certain circumstances, a benefit payable as an annuity under a plan may be provided as a lump sum payment upon plan termination. PBGC regulation 29 CFR 2619.26(b) provides that the present value of the benefit payable in lump sum form must be determined in light of reasonable actuarial assumptions as to interest and mortality. PBGC regulation 29 CFR 2619.26(c)(2) lists several interest rate assumptions which are among those the PBGC will normally consider to be reasonable. The implication of this regulation is that the plan administrator may have a choice as to the interest rate to be used in determining the present value of benefit for the purpose of making lump sum payments. The choice of interest rate will directly affect the amount of the lump sum payments, and thus the amount of plan assets to be allocated to make those payments. Such a determination appears, therefore, to involve discretionary authority over the disposition of plan assets. Consistent with the foregoing analysis, the choice of an interest rate in order to determine the amount of a lump sum payment should be treated as fiduciary activity.

5. **Successor Plans.** Many termination/reversion situations also involve decisions relating to the establishment and design of successor plans after a valid termination. Although such decision may be made as part of the initial decision to terminate the current plan, we believe that the decision of whether to establish a successor plan, and if so, the type for such a plan, are clearly business decisions not subject to Title I of ERISA. As in the case of the decision to terminate, the decision to establish a successor plan involves the exercise of wholly voluntary settlor functions. Similarly, decisions about the design and provisions of any successor plan are not subject to Title I.

As noted above, a more detailed analysis of issues arising in this area may be possible only in the presence of a concrete factual situation. Even under such conditions, the Department may not be in a position to opine on questions such as the prudence of specific courses of activity. In any event, we hope that this general analysis will be helpful to the Advisory Council Task Force in its deliberations.

Sincerely,

Dennis M. Kass
Assistant Secretary

STANDARD TERMINATION AUDIT LETTER

PBGC Case:
EIN/PN:
Plan Name:
Address

Dear Mr.:

ERISA requires that PBGC audit a sample of plan terminations each year, and we have selected your plan termination for audit. Please send me the information on the attached checklist within 30 days. Photocopies are fine. Please return a copy of the checklist indicating the information that is being provided. If any items listed do not apply to your plan, just make a note to that effect.

During the course of the audit, I will calculate benefits, reconcile assets, value lump-sum distributions, verify missing participant information, and confirm distributions and participant information. I have listed all documents I think are necessary to complete the audit. During the course of the audit, additional information may be requested. If you feel other documents would be helpful, please send them.

If you have any of this information in an electronic format, please call me to see if your format is compatible with my system. If you do not already have the information electronically and you have a large number of participants, you may call me to let me know if you will need additional time to submit the information.

If you have any questions at any time, you may contact me at the toll-free telephone number listed below or by e-mail at XXXXXXXXXXX@pbgc.gov.

Sincerely,

XXXXXXXXX, Auditor
Compliance and Audits Branch, Suite 930
1-800-736-2444, ext. XXXX

cc:

Distribution Information

1. _____ **Distribution Summary**

List ALL participants who received a distribution from the Plan through the Date of (Final) Distribution. Show **name, address, gross amount, form**, and **the date of distribution** for each. **Please include the participants who received lump sum distributions, those who did not receive a distribution (deemed cashout of $0) and those participants for whom annuities were purchased. Please provide totals of participant count and amount distributed on listings provided. If this number is different than the number on the PBGC Form 500 and 501, provide an explanation (see item 2).**

2. _____ **Participant/Distribution Reconciliation**

1. Enter the number of participants on the distribution list you are providing _____
2. Enter the total dollar amount paid to participants shown on distribution list you are providing: $_____
3. Do these numbers agree with the participant count and total distribution amount shown on PBGC Form 501(Post Distribution Certification) previously filed with PBGC?
   Yes _____No_____(Please check one)
4. If you checked **No**, you must **reconcile** the number in 2 - (1) and (2) above with the numbers reported on the PBGC Form 501 and provide a revised PBGC Form 501 which reflects the number of participants and total distribution amount as reconciled.
5. Also, if the **final** participant count is **different** than the participant count originally reported on PBGC Form 500 (Standard Termination Notice), you must provide an explanation for the change in the number of participants.

Asset Information

3. _____ **Financial Institution Statements of Assets and Related Cash Flows for All Pension Plan Related Accounts**

Provide bank statements and/or trust statements from date of plan termination through date of last distribution of plan assets that reflect the fair market value of all assets that were available to pay plan benefits and expenses **after** DOPT. These statements should show all cash receipts and disbursements from DOPT through date of last distribution of plan assets including the amount, if any, that reverted to the employer.

If the **Total Dollar Amount** paid in distributions documented in these statements differs from the above **Distribution Summary** or from the **Total** reported in **10e** on PBGC Form 501, you must provide a detailed explanation and reconciliation.

Enter the amount of excess assets that reverted to the employer: $_____
Enter the amount of excess assets used in funding of another plan: $_____
(Please enter a "0" if there was no reversion and/or contribution to another plan)

Plan Information

4. _____ **Plan Documents**
Provide executed plan (with any amendments), prototype, and trust documents. Prior plan documents must be provided if a participant=s benefit was computed under a previous plan document, or if the current plan document was adopted within five years of the date of plan termination (*e.g., date of plan termination 12/1/96, plan effective 1/1/89, plan executed 12/1/93; plan in effect from 12/1/93-12/1/96, 3 years--prior plan document required. If this plan is a replacement of a prior plan, provide copies of the prior plan document).*

5. _____ **Collective Bargaining Agreement** (*provide agreement in effect on the date of plan termination if pension plan was subject to bargaining)*

6. _____ **Most Recent Actuarial Valuation**

7. _____ **Most recent IRS Determination Letter Received**

8. _____ **Excess Asset Allocation Methodology for Mandatory Employee Cont. Plans**
This is required if the plan had mandatory employee contributions and there was a **reversion** of assets to the employer. *The allocation must include any individual who received a lump sum payment of his nonforfeitable benefit during the 3-year period ending with the termination date, if all or part of the participant=s nonforfeitable benefit was attributable to their mandatory contributions.*

Participant Information

9. _____ **Enrolled Actuary's Worksheet**
Provide, in detail, the calculation and valuation of the plan benefits for plans with 25 or less participants (*refer to the attached Participant Data Elements).* For larger plans, you may wait until we have chosen a sample of participants for our audit. This information may be provided in electronic format.

10. _____ **Participant Documentation (provide for sample participants only)**
For plans with less than twenty-five (25) participants please provide (*for larger plans **please wait** until we have chosen a sample of participants for our audit*):
a) Individual Participant Calculation Sheets
b) Executed Benefit Election Forms
c) Executed Spousal Consent Forms
d) Notice of Plan Benefits

11. _____ **Dated Copy of Notice of Intent to Terminate**

12. _____ **Dated Copy of Section 204(h) Notice** (must be provided for significant changes that reduced the rate of future benefit accruals; e.g., benefit accrual freeze, elimination/reduction of early retirement benefits, change in benefit formula, retirement age, etc.)

Insurer/Annuity Provider Information

13. _____ **Group Annuity Contract** (provide copy of contract used to fund plan, if applicable, as well as, annuity contract purchased to provide plan benefits upon plan termination)

The contract must include all options available under the contract, the name of the annuitants, their monthly benefit amount, and form of payment (include certificates if available).

14. _____ Notice to Participants of Actual/Proposed Insurer

Participant Data Elements

The Enrolled Actuary's Worksheet should include, but not be limited to, the information below as it applies to the plan for each active, retired, terminated vested participant and beneficiaries and alternate payees.

(4) Name
(5) Date of Birth
(6) Date of Hire
(7) Date of Participation
(8) Yearly Compensation History as defined by the Plan and Average Compensation used in the determination of plan benefits
(9) Age used to determine lump sum value *(indicate if age nearest birthday, attained age or age at last birthday)*
(10) Accrual Service *(state whether service based on total years of service or participation and provide dates of any breaks-in service, if service is based on hours worked, provide the number of hours worked in each accrual period)*
(11) Accrual Fraction and any other relevant factors *(e.g., service reduction factors, benefit conversion factors, etc.)*
(12) Normal Retirement Benefit
(13) Accrued Benefit
(14) Terminated Vested Participants *(provide date of termination of employment, vesting service and vesting percentage)*
(15) Retired Participants *(provide date of retirement, form, spouse's date of birth if applicable and benefit amount)*
(16) Interest Rate and Mortality Table used to determine lump sum distribution *(indicate if post-retirement mortality only or pre and post retirement mortality was used)*
(17) Top Heavy Minimum Benefits, if applicable *(include the years that the plan was top heavy, top heavy service compensation, and the factor used to convert top heavy percentage to normal form of benefit)*
(18) Amount of employee contributions with and without interest
(19) Estimated primary social security benefit or covered compensation *(include a worksheet illustrating PIA computation; if covered compensation is used in the determination of a benefit, provide the Year of the Compensation Table and indicate whether Table I or Table II is used in the benefit determination)*

SAMPLE PREMIUM AUDIT LETTER FROM PBGC

Date XX, 2005

Ms. Plan Administrator
Company
Street Address
City, State XXXXX
Re: Premium Compliance Evaluation of Pension Plan
EIN/PN XX-XXXXXXX/XXX
For the Plan Year Commencing Month XX, 200X

Dear Ms. Plan Administrator:

As Ms. Plan Administrator discussed with XXXXXXXX of our office today, we have selected the subject plan for evaluation as part of our Premium Compliance Evaluation Program (see the attached Fact Sheet or 29 CFR Chapter XL, § 4007.10 of PBGC's premium regulations on PBGC's website at www.pbgc.gov). The primary emphasis of our evaluation will be to assess documentation supporting the fixed rate premium and the variable premium reported on the attached PBGC Form 1 filing for the plan year commencing Month XX, 200X.

To help us plan our evaluation, we would appreciate your sending the information requested in the attached listing by Month XX, 2005. Please cross-reference the documents that you are submitting to the attached initial information request listing and send this information to:

Premium Compliance Evaluation Program
Contracts and Controls Review Department/Suite 580
Pension Benefit Guaranty Corporation
1200 K St., N.W
Washington, D.C. 20005-4026

After we have reviewed this information, we will contact you to discuss it, seek any additional information or clarifications needed about the plan and its administration, and provide you with an opportunity to ask any questions you may have about our evaluation process. We will then make an initial assessment as to what additional steps will be necessary, including whether we should close the evaluation based on the information you will have already provided. Depending on that assessment, we may determine that we need to visit your organization to review participant records or other source documentation. For your information, we may also ask a CPA firm, authorized by our agency to support this program, to assist us in our evaluation.

We look forward to working with you and completing our evaluation in an efficient and timely manner. If you have any questions or if you have difficulty in compiling the information requested, please contact me at (202) 326-4161 at ext. XXX. We will be happy to discuss with you the most efficient way to help us obtain the needed information or address any other concerns you may have with the process.

Sincerely,

Attachments:

Initial Information Request
2002 PBGC Form 1-EZ Premium Filing
PBGC Facts Sheet on PCE Program

Initial Information Request

A. Background Information

1. A brief history of the plan, including any mergers, acquisitions, or spin-offs
2. An organizational chart that identifies the unit(s), which employ the plan's participants
3. The names and locations of the units identified in the organization chart and for the plan year under review, the number of employees for each applicable unit
4. An indication of the extent to which the units' employees are covered by another pension benefit plan
5. Internal auditors' and independent accountants' reports on the pension plan's activities, internal controls and financial statements that were issued for (a) the preceding plan year, (b) the plan year under review, and during (c) the period from the end of the plan year under review to the date of this request.

B. Plan Documents

1. An executed copy of the original plan document or latest restatement and all subsequent amendments effective through the snapshot date of May 31, 2002.

C. Determination of Participant Count

1. A narrative for the plan year under review that explains how the plan participant count, per the PBGC Form 1, was derived, including how the number was calculated for applicable classifications, such as current employees, leased employees, affiliated service group employees, inactive individuals (retirees and deferred vesteds), and deceased individuals with beneficiaries
2. Electronic files for the following supporting documentation:

- Listings of plan participants for each applicable classification (e.g. actives, deferred vesteds, retirees)
- W-2 census data for employees who worked during the year preceding the plan year under review
- Form 1099-R listings of retirees and beneficiaries who are receiving benefits.

D. Payroll Processing

1. A narrative that:

- Describes the sponsor's payroll processing system and supporting personnel records
- Indicates whether the sponsor's payroll system is (a) centralized or decentralized and (b) manual or automated
- Describes, if the payroll system is automated, the extent to which it is operated in an integrated fashion and linked electronically with the pension plan's financial and administrative system(s)

2. The locations of the sponsor's payroll / human resources processing centers.

E. Actuarial Valuation and Assumptions

1. The Actuarial Valuation Report for the 2002 plan year under review, the 2001 plan year, and the 2000 plan year.
2. An indication of the availability of actuarial calculation worksheets and supporting records.

F. Department of Labor/IRS Form(s)

1. IRS Form 6559, Transmitter Report of Magnetic Media Filing (which establishes the number of W-2s that were issued) for the year preceding the plan year under review or the in-house header information from the payroll tapes to justify the total payroll count
2. DOL/IRS Form 5500 including all required attachments for the 2002 plan year under review, the 2001 plan year, and the 2000 plan year.

SAMPLE PARTICIPANT NOTICE AUDIT LETTER FROM PBGC

Date XX, 2005

Ms. Plan Administrator
Company
Street Address
City, State XXXXX
Re: Participant Notice Compliance Evaluation Program

Dear Ms. Plan Administrator:
We regularly review selected PBGC Form 1 filings to assess compliance with Section 4011 of ERISA and 29 CFR Part 4011 as part of PBGC's Participant Notice Compliance Evaluation Program. We have selected the subject filings for further evaluation (see attachments). Our records indicate that the 2003 PBGC Form 1 filing contains a certification that a Participant Notice was not required to be issued for the 2002 plan year.

Based on our preliminary analysis of database information obtained from PBGC Form 1 and Form 5500 filings, we believe that the subject plan may have been required to issue Participant Notices for the 2002 plan year. However, before we make an initial determination regarding your compliance with this requirement, we would like to give you an opportunity to review your compliance with the Participant Notice requirements.

If a notice was issued for the subject plan year, please provide a copy of the notice, the date of its distribution, and update your certification using the attached Participant Notice Certfication Worksheet. If a notice was not issued and you agree that it should have been issued, please issue the notice. In addition, please provide us a copy of the notice, the date of its distribution, and update your certification using the Participant Notice Certification Worksheet. If a notice was not issued and you believe it was not required, please provide the basis for your position along with any documentation which supports your conclusion.

We request that you submit your response to the following address by XX-XX-XX.

****

Single employer plans that are covered by the PBGC's pension insurance program are generally required to issue a Participant Notice for a plan year if a variable rate premium is payable for that plan year, unless a funding-related test is met. For your information, we have attached PBGC's Technical Update 02-2 (2002 Model Participant Notice), which contains a worksheet for determining whether Participant Notices were required for the 2002 plan year. This technical update and PBGC's regulation on Participant Notices are available at PBGC's website, www.pbgc.gov. Failure to issue a Participant Notice in a timely manner may result in the application of penalties under Section 4071 of ERISA.

If you have questions regarding this letter or believe you have received this letter in error, please contact at [ ].
Sincerely,

Attachments:
2002 Participant Notice Certification Worksheet
2003 PBGC Form 1 filings
2004 PBGC Form 1 filings
PBGC Technical Update 02-2

APPENDIX C - FEDERAL GOVERNMENT TELEPHONE NUMBERS

PENSION BENEFIT GUARANTY CORPORATION	NAME	Area code 202
Executive Director	Bradley Belt	326-4010
Deputy Executive Director &Office of Policy and External Affairs	Vince Snowbarger	326-4010
Chief Financial Officer	James Gerber	326-4170
Chief Administrative Officer	Steven Barber	326-4180
General Counsel	Judith Starr	326-4020
Director, Benefit Administration and Payment Department	Bennie Hagans	326-4050
Director, Insurance Program Department	Terry Deneen	326-4020
Chief Counsel	Jeff Cohen	326-4020
Manger, Standard Termination Compliance Division	Bella Pelli	326-4000
Manager, Actuarial Services Division & Chief Financial Actuary	Joan Weiss	326-4051
Manager, Actuarial Policy Division and Chief Policy Actuary	Dave Gustafson	326-4080
Chief Negotiations Actuary		326-4070
Chief Research Actuary	Jane Pacelli	326-4080
Problem Resolution Officer – Practitioner Problems	Diane Morstein	326-4061
Problem Resolution Officer - Participant Problems	Ondrea Gill	326-4006

INTERNAL REVENUE SERVICE	NAME	
Commissioner, Tax Exempt & Government Entities Assistant Commissioner, TE/GE	Steve Miller Sarah Hall-Ingram	
Director, Employee Plans	Carol Gold	
Director, Employee Plans Rulings and Agreements	Joe Grant	
Manager, EP Technical Guidance & Quality Assurance	Martin Pippins	
Manager, EP Technical	Jim Holland	
Actuarial Branch Chiefs	Donna Prestia	
Employee Plans Customer Account Services http://www.irs.gov/retirement/article/0,,id=96919,00.html	Go to website listed in left-hand column	877-829-5500
Employee Plans Assistance RetirementPlanComments@irs.gov	Voice Mail	283-9660

DOL's Employee Benefit Security Administration	NAME	Area code 202
Assistant Secretary	Ann Combs	693.8300
Deputy Assistant Secretary for Program Policy	Brad Campbell	693.8300
Deputy Assistant Secretary for Program Operations	Alan Lebowitz	693.8315
Director of Exemption Determinations	Ivan Strasfeld	693.8540
Director of Policy and Research	Joseph Piacentini	693.8410
Director of Enforcement	Virginia Smith	693.8840
Director, Program Planning, Evaluation and Management	Brian McDonnell	693.8480
Director of Regulations and Interpretations	Robert Doyle	693.8500
Chief, Division of Fiduciary Interpretations and Regulations	Lou Campagna	693.8512
Chief, Division of Coverage, Reporting, and Disclosure	Joe Canary	693.8531
Chief Accountant	Ian Dingwall	693.8360
Executive Secretary, ERISA Advisory Council	Larry Good	693.8668
Chief Actuary	Zenaida Samaniego	693.8438
Public Disclosure (to request filed SARs & SPDs)	Gloria Davis	693.8678
Division of Participant Assistance and Inquiries	Sharon Watson	693.8630

APPENDIX D: Bibliography and Useful Websites

ERISA & Regulations (especially Title IV)
http://www4.law.cornell.edu/uscode/html/uscode29/usc_sup_01_29_10_18.html
Internal Revenue Code & Regulations (Pension Benefit sections)
http://www4.law.cornell.edu/uscode/html/uscode26/usc_sup_01_26_10_A_20_1_30_D.html
MPPAA, SEPPA, PPA87 (in OBRA87), RPA94: Law, Committee Reports, and Analysis
http://thomas.loc.gov/bss/d109/d109laws.html locate using table of PL numbers in Chapter I of study note.
BNA Tax Management Portfolios: Terminations

PBGC Forms and Instructions found at www.pbgc.gov/practitioners/index.html or by calling 202-326-4000)
PBGC Standard Termination Forms 500, 501, EA-S, REP-S, and Instructions
PBGC Distress Termination Forms 600, 601, 602, EA-D, REP-D, and Instructions
PBGC Premium Forms 1, 1-ES, 1-EZ, Schedule A, and Instructions and My PAA (PBGC's E-filing system)
PBGC Notice of Reportable Events: Form 10 for post-event and Form 10-A for Advance Notice
PBGC Notice of Failure to Make Required Contributions over $1 Million
PBGC Missing Participant Filing Schedule MP and instructions

Other PBGC material for Practitioners (Laws, Regulations, Guidance, R&D, Statistics, Information on Premiums, Terminations, Multiemployer Plans, and Interest Rates) can be found at:
http://www.pbgc.gov/practitioners/index.html

IRS Forms and Instructions can be found on the Internet at www.irs.gov/formspubs/index.html
All the IRS Form 5300 series for Determinations, such as:
Form 5310 - Application for Determination Upon Termination
Form 5310A - Notice of Plan Merger or Consolidation, Spinoff, or Transfer of Plans Assets or Liabilities
All the IRS Form 5500 series for the Annual Report/Return of Employee Benefit Plan, such as Schedule B
Form 6088 - Distributable Benefits from Employee Pension Benefit Plans
Form 8717 - User Fee for Employee Plan Determination Letter Request
Other forms for EP (Exempt Plans) can be found at http://www.irs.gov/retirement/article/0,,id=96763,00.html

Other IRS Information:
Published Guidance: http://www.irs.gov/retirement/content/0,,id=96710,00.html
Other Information for Practitioners: http://www.irs.gov/retirement/practitioner/index.html
Other Information for Plan Sponsors: http://www.irs.gov/retirement/sponsor/index.html
Internal Revenue Bulletins (providing Regulations, Revenue Rulings, Revenue Procedures, Treasury Decisions, Notices, Announcements, etc.) http://www.irs.gov/businesses/lists/0,,id=98230,00.html

DOL's Employee Benefits Security Administration

Rules and Regulations in Title 29 Chapter 25: http://www.dol.gov/dol/allcfr/ebsa/Title_29/Chapter_XXV.htm
Other EBSA Rules: http://www.dol.gov/ebsa/regs/main.html
Interpretive Bulletins: http://www.dol.gov/dol/allcfr/Title_29/Part_2509/toc.htm
Interpretive Bulletin 95-1 relating to the fiduciary standard under ERISA when selecting an annuity provider
http://www.dol.gov/dol/allcfr/Title_29/Part_2509/29CFR2509.95-1.htm
Advisory Opinions http://www.dol.gov/ebsa/regs/AOs/main.html