Recent Pension Law Changes and PBGC Enforcement Decisions Impact Certain Corporate Transactions

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Year End Change Impacting Employers Sponsoring Defined Benefit Pension Plans in the Group of Controlled Companies

The Pension Benefit Guaranty Corporation (the "PBGC") has had a number of tools which it has been able to use to intervene in transactions of employers sponsoring defined benefit pension plans ("DB Plans") to protect itself from having what it considered to be unreasonable increases in its liabilities for guaranteeing the pension benefits under such plans. Those tools were used in a number of corporate transactions when the PBGC determined that the transaction was likely to unreasonably increase it liabilities due to the employer's DB Plan(s) being underfunded (on a termination basis), the employer's financial situation being a bit precarious and the PBGC was concerned that the corporate transaction was moving assets outside of the controlled group of companies which included the employer sponsoring the DB Plan (for example, when a subsidiary was spun off or a corporation was split into two entities that were no longer going to be commonly controlled).

One of the tools used by the PBGC, was a section of ERISA that permitted the PBGC to take action against an employer who ceased operations at a facility in a manner that resulted in more than 20% of the participants in the employer's DB Plan ceasing to participate in the plan and separating from employment with the employer which triggered certain liabilities and reporting obligations under ERISA. The PBGC had placed a moratorium on its enforcement of such provision last July while it worked on ways to minimize the impact of its investigations on these business transactions. Late last year Congress enacted a law making major changes to this section of ERISA. The PBGC is reviewing the new section and has decided the enforcement moratorium on this section it issued last July is now lifted and this means that the PBGC may again be issuing requests for information to corporations engaging in certain corporate transactions which can slow or even terminate the progression of the transaction.. The catch is that on January 8, 2015, the PBGC lifted its enforcement moratorium on this section and announced enforcement of the newly enacted section on employers that had or have a cessation of operations on or after December 16, 2014 if such cessation of operations is not exempt under the new section. If your company engaged in a corporate transaction on or after December 16, 2014 and there was a DB Plan maintained in the controlled group of corporations, the PBGC's non-enforcement position is no longer applicable and you may receive a request for information about that transaction from the PBGC. This is separate and distinct from an employer's obligation to report certain corporate transactions to the PBGC when they maintain a DB Plan.

The new section generally applies to corporate transaction or changes when there is a substantial cessation of operations at a facility which results in a workforce reduction of the number of employees eligible to participate in any retirement plan of more than 15% (defined benefit and any defined contribution plan such as a 401(k) plan or any nonqualified plan that defers payment until termination of employment that is not exempt as a top-hat plan). The reduction is measured against the number of all eligible employees to participate in any such retirement plan as compared to the number eligible immediately before the earlier of the date of the employer's decision to implement the cessation of operations at a facility or workforce reduction, or if the permanent cessation of operations occurred over a 3 year period, then the separations from employment for the 3 preceding years are aggregated to determine if the more than 15% threshold is met. Certain corporate transactions are not treated as cessations of operations if a number of conditions are satisfied, so each transaction must be analyzed to determine if it constitutes a cessation of operations subject to the new requirements. There are many provisions in the statutory provisions summarized at a high level in this paragraph that still require interpretation and guidance.

While the PBGC is reviewing the new statutory provisions, the notice repealing the PBGC's enforcement moratorium included a reminder that the following "cessations of operations" are exempt under the new statute:

- Plans with fewer than 100 participants are not required to report a cessation of operation.
- Plans that are funded at 90% or greater level when the plan's assets are compared to its unfunded vested benefits.

A DB Plan that meets one of the two bullet point exemptions is not required to report its cessation of operations to the PBGC. This is a separate reporting obligation from the reporting required for "reportable events" by a DB Plan sponsor. Any other plan sponsor of a DB Plan that has a cessation of operations is still required to report the corporate transaction or facility closure that meets the cessation of operations of more than15% threshold. Depending upon the event that occurs, an employer may need to report the new event as a reportable event within 30 days of occurrence, or as a reportable event if liabilities for vested benefits exceed a certain amount in advance of the transaction, and annually in a report on events under the section. If the cessation is more than 15% but less than 20%, it is also possible that only the annual report will be required, but each situation must be analyzed carefully under the reportable event requirements and under section 4062 to determine which reports are required and when. For transactions that involved a reduction in the number of participants in retirement plans that closed on or after December 16, 2014, employers should carefully review whether there is a reporting obligation and when each type of report is or may be due for the transaction since the new reporting requirement is not limited to reductions in DB Plan participants, but now includes reduction in all retirement plan participants.

The new rules will apply to cessations in operation occurring on or after December 16, 2014 unless a settlement agreement was entered into before June 1, 2014. If your company has a cessation in operations that meets the new more than 15% threshold, there is a new way to satisfy the liability for the employer's DB Plans' unfunded vested benefits at the cessation that is intended to be less expensive by requiring the company to contribute an amount equal to 1/7th of the unfunded vested benefits in 7 annual installments to the DB Plan. The 7 annual installments stop when the plan hits 90% funding of its unfunded vested benefits and this ends the installments even if the funding later drops below 90%. Failure to make any required payment accelerate the remaining payments.

The PBGC will continue its prior enforcement policy (2012) and will not enforce this section of the law against any company that is financially sound. Any pre-June 1, 2014 settlement under section 4062(e) will still be enforced. The PBGC's prior enforcement policy (October 2012) exempted "strong company" cases, and new small plan cases where there were less than 100 participants on which the plan paid the PBGC flat rate premium. To remain outside of PBGC current and prior enforcement policies, a company must be a strong company which is a company that either (1) has an unsecured debt equivalent rating from Moody's of Baa3 and/.or from S&P of at least BBB-; or (2) the company is not rated by Moody's or S&P, but it has a D& B Financial Stress Score of 1477 or higher and the company's secured debt (other than debt to buy real estate or equipment) does not exceed 10 percent of its asset value. However, under the 2012 enforcement policy, the PBGC still had the discretion to determine that such a company is not financially sound if in its judgment there are signs of financial weakness or it has an insignificant amount of assets or operations in the U.S.

Employers who sponsor DB Plans that are less than 90% funded who are engaged in corporate transactions or who are considering stopping operations at a facility should consider how the newly revised Section 4062(e) of ERISA may impact the financial ramifications of such decisions.

Year End Changes Impacting Employers that Contract with Unions Providing Multiemployer Pension (Defined Benefit) Plans

Late in December, changes to the funding requirements for multiemployer pension plans maintained by unions were also enacted. Some of those changes merely extended the Pension Protection Act of 2006 funding rules for another year until December 31, 2015, but the change also extended the time period in which multiemployer plans can apply for extensions in amortization periods used to calculate their funding obligations until December 31, 2015. Companies who have negotiated collective bargaining agreements with unions maintaining multiemployer plans and companies considering purchasing entities with collective bargaining agreements with unions maintaining multiemployer plans (e.g., employers in industries such as plumbers and pipefitters, electrical workers, the motion picture industry, construction, trucking and transportation, and the hospitality industry for a few) will want to request more information regarding the funded status of these union sponsored plans and the elections the plans have made which impact the funding of such plans since the employer is contractually bound to make contributions while the contract is in place and probably when they withdraw from the contract and the union plan's funded status and elections impacting funding will impact the employer's financial obligations currently and when they withdraw from the union contract.

Under the new multiemployer plan rules, the PBGC premium has doubled from $13 to $26 per participant beginning in 2015.

Multiemployer plans under the Pension Protection Act of 2006 were categorized by their funded (or underfunded status) into four categories to which practitioners generally assigned colors:

- Green- non-problematic currently
- Yellow-endangered
- Orange- seriously endangered
- Red- critical

Plans that were in the yellow and orange zones were to adopt funding improvement plans to improve their funding and plans in the red zone were to adopt similar plans called rehabilitation plans and these plans could be accomplished by increasing employer contributions or reducing future benefit accruals and for plans in the red zone they could also reduce early retirement and death benefits. The new changes go further and permit in some cases reduction of accrued benefits, including benefits in pay status (e.g., reducing a retired employee's monthly pension payment).

The law adds a new 5th category for plans funded in the red category and who are in worse shape, the "critical and declining category". These are plans projected to be insolvent within 14 years or within 19 years if more than two-thirds of the participants are inactive or retired or if the funded status is less than 80%. These plans can suspend benefits for a period or permanently. There are a number of conditions on such suspensions, but most suspensions will require participant consent,

The multiemployer plan has the ability to elect to downgrade its funding status if it is projected that it will be in critical funding status within five years that enables the union to increase employer contributions and reduce early retirement and death benefits sooner rather than waiting for the critical status to develop. There are also new provisions permitting the union to impose a revised funding schedule when negotiations toward a new collective bargaining agreement which includes a funding or contribution schedule as part of the multiemployer DB plan's rehabilitation plan to improve its funding status from critical/red status is not agreed to in negotiations with the employer if a new schedule is not agreed upon by the date that is 180 days after the most recent collective bargaining agreement expired while the plan was in critical/red status.

Plans in the red zone have an automatic 5% increase or surcharge on the amounts employers pay, and the changes clarify that this surcharge is not used to calculate the employer's withdrawal liability. This is important because the two highest years of the employer's contributions to the multiemployer plan is an element in calculating withdrawal liability. Similarly any contribution increases as part of a funding improvement plan or a rehabilitation plan are now clearly not included in calculation of the withdrawal liability. However, not everything in the law is good, and the law does not permit the withdrawal liability to consider any benefit reductions implemented to improve funding which means an employer pays a portion of the withdrawal liability to the multiemployer plan related to funding of benefits that no participant is likely to ever receive.

Employers bound by collective bargaining agreements that include multiemployer pension plan contribution obligations will want to continue to monitor the funding status of the multiemployer pension plan and request notification of any funding elections or other elections the union may make with respect to the multiemployer pension plan to monitor its potential obligations with respect to such plan. Plan actuaries are required to currently certify in the annual valuation whether the multiemployer plan is currently in endangered or critical status; however, the law has changed the certification to require that it also state whether the plan is or will be in critical status for the next year or in any of the next five plan years so review of the actuarial certifications on multiemployer plans beginning with the plan year beginning after December 31, 2014 will provide information on the projected funding status of the plan and until then, companies will need to make requests for such information since it will not be included in the actuarial certifications currently available for 2014 and earlier. Companies considering acquiring entities bound by collectively bargained multiemployer pension plan obligations should request actuarial reports on any such plan and details regarding the funding status, funding status projections for the plan for the next 5 years and any elections made with respect to the funding of such plan before and after December 31, 2014.

Employers contracting with multiemployer plans now also have expanded access to the multiemployer plan documents, rehabilitation plans, funding improvement plans and funding notices under the new changes effective for plan years beginning after December 31, 2014. The access is available by providing the union sponsoring the multiemployer plan with a written request; however, only actuarial reports in the union's hands for more than 30 days are subject to the disclosure requirement.. Only one copy is required to be provided in any 12 month period, so employers may want to carefully consider the timing of their request to obtain the most recent data available.

Some of the changes for critical and declining status multiemployer DB Plans were effective as of the date of enactment, December 16, 2014. One such change is a requirement that the annual funding notice of the multiemployer DB Plan include new additional information if the plan is in a critical and declining status. This additional information includes information regarding the projected date of the plan's insolvency, a statement that insolvency may result in benefit reductions and a statement regarding whether the plan sponsor (union maintaining the plan) has taken legally permitted actions to prevent the insolvency. Annual funding notices issued after December 16, 2014 should be requested as part of due diligence in any corporate transaction involving a multiemployer DB plan.