Pension Benefit Guaranty Corporation

75-2

April 4, 1975

OPINION:

Dear Congressman:

The Internal Revenue Service has referred to this Corporation your request for comments on the inquiry of your constituent * * *, concerning the applicability of the plan termination insurance provisions of the Employee Retirement Income Security Act of 1974 ("ERISA" or the "Act") to a pension plan funded by the purchase of annuities from a private insurance company with the policies individually issued to plan participants. Other Members of Congress have asked for comments on similar inquiries from Mr. * * *, and the following statement reflects our previous responses.

Section 4021 of ERISA established the scope of the Act's termination insurance provisions. With certain enumerated exceptions, coverage extends to any defined benefit employee pension plan which has met the requirements of the Internal Revenue Code governing "qualified" plans. As Mr. * * * correctly noted, there is no exclusion from coverage (and, thus from the premium payment obligation) for defined benefit plans which are funded by the purchase of private insurance policies. Of course, even plans funded by insurance policies present some risk to the Corporation, since the Corporation would be obligated to pay benefits upon termination of such a plan if it had failed to pay premiums to its private insurer, or if that insurer became insolvent.

More to the point, Mr. * * * objection to paying premiums of the Corporation reflects his erroneous assumption that that obligation reflects the traditional "risk spreading" insurance concept. But, ERISA is not comparable to traditional insurance programs. Thus, the initial premium payment obligation is unrelated to the risk of plan termination and does not "buy" protection. On the contrary, the Corporation must guarantee benefits even if an administrator fails to pay premiums. (See Act §4007(d).) And, Congress has characterized the purposes of the Act in social terms, i.e., to "protect interstate commerce, the Federal taxing power, and the interests of participants in private pension plans and their beneficiaries," and has expressly found "that owing to the termination of plans before requisite funds have been accumulated, employees and their beneficiaries have been deprived of anticipated benefits . . ." (See Act §2(a) and (c).) In establishing the plan termination insurance program, therefore, Congress determined that the pension plan "industry" should bear the burden of financing the program. Indeed, the original Senate version of ERISA would have imposed the premiums as excise taxes to be collected by the Internal Revenue Service. That concept is closely paralleled in the enacted law, although after September 2, 1975 some plans may elect a lower premium rate based partly on the adequacy of plan assets. (See Act §4006(a).) Thus, Mr. * * * position may reflect an incomplete understanding of the statutory scheme.

Finally, we note that Mr. * * * has described his firm's plan as an "individual account" plan. Such plans are specifically excluded from the termination insurance provisions of ERISA. (See Act ? 4021(b)(1).) Whether Mr. * * * plan is in fact an individual account plan depends upon whether the plan satisfies the provisions of ? 3(34) of the Act, which defines the term individual account plan. But, it may be that his plan is not obligated to pay premiums, a matter which we would be glad to consider if Mr. * * * requests a ruling from our General Counsel.

I hope the above discussion will be of assistance to you in responding to Mr. * * *

Steven E. Schanes

Acting Executive Director