Pension Benefit Guaranty Corporation

81-11

May 11, 1981

REFERENCE:
4041 Termination by Plan Administrator
4047 Restoration of Plans
4048 Date of Termination
4062 Liability of Employer in Single Employer Plans

OPINION:

This is in response to your inquiries and confirms the oral advice I gave you on April 27, 1981, concerning the proposed termination of the * * * Hourly Rate Employees' Pension Plan (the "Hourly Plan"), and the Amended and Restated Supplementary Benefits Agreement (the "Supplemental Agreement") that * * * proposes to adopt in the future. In brief, the Supplemental Agreement will provide a target benefit pension plan and certain other retirement benefits for current employees. Moreover, a side-letter agreement between.

* * * (the "Union") would assure that no participant's benefits would be diminished as a result of the Hourly Plan's termination. You have asked whether the adoption of these arrangements will affect the proposed termination of the Hourly Plan. As more fully explained below, the Pension Benefit Guaranty Corporation ("PBGC") has determined, based on all the information disclosed, that under the circumstances you have presented to us, the Hourly Plan should not be treated as terminated [*2] under Section 4041 of the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), 29 U.S.C. § 1341.

* * * filed a Notice of Intent to Terminate with PBGC on October 19, 1979 and proposed a date of termination of October 31, 1979. Decuments enclosed with the Notice of Intent to Terminate indicate, based on our review, that the plan asset insufficiency of the Hourly Plan on the proposed date of termination is over $4,000,000. Further, other documents enclosed with the Notice appear to indicate that * * * may have had little, if any, net worth as of the proposed date of termination and during the preceding 120 days, so that employer liability amounts calculated under Section 4062 of ERISA, 29 U.S.C. § 1362, may be substantially less than the plan asset insufficiency. Additionally, it appears that * * * intends to continue operating as an ongoing business with the same products and the same employees.

It is clear that your total proposal contemplates the use of PBGC's guaranteed benefit payments as a constituent element of a redesigned, ongoing retirement program. The redesigned program would transfer a large liability from * * * to the PBGC, while providing substantially [*3] similar, if not greater, benefits to present and future employees and retirees subsequent to the purported termination of the Hourly Plan as would have been the case absent such termination. To accomplish this result, * * * proposes to adopt and implement the various elements of the * * * Supplemental Agreement: the * * * Target Benefit Plan (the "Target Plan"), a disability insurance plan, a severance pay plan, additional group life insurance benefits, and the side-letter agreement. The Supplemental Agreement would have an effective date of October 7, 1980. As we understand it, the Target Plan would be established for current employees of * * *. The targeted benefit would be greater than that provided under the Hourly Plan at the time of its termination. Contributions to each individual participant account would be computed so that the account balance at the participant's normal retirement date (age 65) would provide the targeted benefits.

For current employees of * * * who were vested under the Hourly Plan, the Target Plan would provide benefit credit for service after February 1, 1977. Moreover, for current employees who were not vested under the Hourly Plan, the Target [*4] Plan would also provide credit for all past service and would require funding of such a participant's account for such service.

Also, for current employees, the disability insurance, severance pay, and additional life insurance plans in the Supplemental Agreement would provide benefits which were included under the Hourly Plan and which would otherwise have been lost because of the termination of that Plan.

The proposed side-letter agreement recites that the foregoing arrangements are intended to assure that Hourly Plan participants receive at least the same benefits as those provided by the Hourly Plan, and provides that * * * will make up the difference in any case where the combination of new plans and PBGC guarantee payments inadvertently results in a diminished benefit. n1

n1 We understand that the proposed side-letter agreement is intended to replace, but have the same effect as the following "Intent" provision from an earlier version of the Supplemental Agreement:

"It is the intent of the parties hereto that no [Hourly Plan] participant (or any intended beneficiaries of any such person) shall sustain a loss or diminution of benefits by virtue of the termination of the [Hourly Plan]. The Target Benefit Plan, together with amounts received under the [Hourly Plan] pursuant to Title IV of ERISA and the amounts payable [for early retirement, surviving spouse coverage and disability benefits], is intended to provide benefits that will in no event be less than those to which employees, retirees and their beneficiaries would have been entitled had the [Hourly Plan] remained in full force and effect through the expiration of this Agreement. In the event that it shall appear that any such person will not receive such undiminished benefits under this combination of programs, whether through inadvertence, miscalculation or otherwise, the Company shall promptly act to remedy any such deficiency." [*5]

Putting these various pieces together -- the Target Plan, the disability, severance pay and insurance plans, the side-letter agreement, and the payment of PBGC guarantees -- it is evident that the total package has been crafted so that retirees and employees, both present and future, will receive benefits as though no termination had occurred. The package has been designed, however, so that PBGC would be funding a major portion of the program's cost, based upon a purported termination of the Hourly Plan.

In our view, the termination insurance program of Title IV was not intended to subsidize an employer's ongoing retirement program. Accordingly, we believe that a purported termination of one plan, contrived in concert with the establishment of new retirement arrangements which are designed to provide substantially the same benefits for the future, should not be treated as a termination within the statutory contemplation so as to require the payment of PBGC guarantees.

If PBGC guarantees were to be paid under such circumstances, then any company whose unfunded liabilities under a defined benefit pension plan exceed 30% of its net worth could find it advantageous to establish [*6] similar arrangements to secure PBGC's payment of the major portion of its costs of an ongoing retirement program. Such a result would have extremely adverse cost consequences for this insurance system. Our review of available data for major corporations whose pension liabilities are reported by Standard & Poor's Compustat service has readily identified over 20 very large firms whose unfunded pension liabilities substantially exceed 30% of their net worth, and whose financial difficulties would undoubtedly make tempting the adoption of arrangements similar to those you are proposing. The combined unfunded pension liabilities of those plans which have been thus identified is approximately $6.0 billion, and PBGC's potential exposure if they were to terminate, based upon net worth estimates, is some $4.1 billion. Thus, the consequences of our acceptance of the type of proposal you are advancing could be either a huge shift of pension costs to PBGC's premium payers, or the total collapse of the insurance system.

We do not believe the statute should be read so narrowly as to require PBGC to accept a result so patently at odds with the legislative purpose -- which is, after all, to protect [*7] the pension expectations of individual retirees and workers, not to provide bail-outs for financially pressed firms -- and so inimical to this program's continuing viability.

For example, Section 4047 of ERISA 29 U.S.C. 1347, provides PBGC with express authority to limit plan terminations. That section states in pertinent part:

Whenever the corporation determines that a plan which is to be terminated, or which is in the process of being terminated, under this subtitle, should not be terminated as a result of such circumstances as the corporation determines to be relevant, the corporation is authorized to cease any activities undertaken to terminate the plan, and to take whatever action is necessary and within its power to restore the plan to its status prior to the determination that the plan was to be terminated. [emphasis added]

The breadth of this provision is further reflected in its additional grant of authority to PBGC to restore to its pretermination status, a plan whose termination has already been completed. In addition, under section 4048 of ERISA, 29 U.S.C. 1348, there is no date of plan termination unless one is agreed to by PBGC (or established by a court). [*8]

Under all of the facts you have presented to us, and for the reasons discussed above, we do not believe it appropriate to agree that a plan termination would occur. In view of the necessity to protect the insurance system from the cost of having its guarantees used to fund an employer's ongoing retirement program, we conclude that the Hourly Plan would not be treated as terminated under the circumstances you have proposed.

Robert E. Nagle
Executive Director