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# Section 4062(e) Liability In Transition: Planning For An Uncertain Future

BY HAROLD J. ASHNER AND DEBORAH WEST

Employers that are downsizing or restructuring should take note of two recent developments that may lead to significant changes in the Pension Benefit Guaranty Corporation's enforcement of Section 4062(e) of the Employee Retirement Income Security Act of 1974.[1] Since 2006, when PBGC promulgated a liability formula rule, 4062(e)—the so-called "downsizing liability" provision—has been a centerpiece of PBGC's enforcement activity. The agency's expansive 4062(e) positions and aggressive enforcement actions have attracted vigorous opposition from employers and trade groups.

In a positive—albeit time-limited—development, on July 8, 2014, PBGC announced a moratorium, from July 8, 2014, to Dec. 31, 2014, on its enforcement of 4062(e) liability.[2] During the moratorium, PBGC said, companies should continue to report new 4062(e) events, but PBGC will cease enforcement efforts regarding both open and new cases.

Shortly after PBGC's moratorium announcement, on July 23, 2014, the Senate Health, Education, Labor and Pensions Committee, by a bipartisan voice vote, approved a bill that would change the statutory provisions governing 4062(e) liability in a number of ways that would render downsizing liability both more predictable and more rational.

Both the PBGC moratorium and the HELP Committee's action, which follow a number of noteworthy 4062(e) developments over the past eight years, appear to reflect an increasing momentum for reform. These two key developments highlight the importance of the need for awareness of—and effective planning regarding—potential 4062(e) issues in a regulatory and legislative environment that could change significantly in the near-term—whether as a result of policy or regulatory changes within PBGC or as a result of the enactment of reform legislation, or some combination of both.

## The Basics of 4062(e) Liability

Section 4062(e) liability arises if "an employer[3] ceases operations at a facility in any location and, as a result of such cessation of operations, more than 20 percent of the total number of his employees who are participants under a plan established and maintained by him are separated from employment."[4] Under PBGC's

[1] 29 U.S.C. § 1362(e).

[2] The announcement was made in a press release, at http://www.pbgc.gov/news/press/releases/pr14-09.html.

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[3] Under ERISA Section 4001(b)(1), 29 U.S.C. § 1301(b)(1), the plan's contributing sponsor and all members of its controlled group are treated together as a single "employer." *See also* ERISA Sections 4001(a)(13) and (a)(14), 29 U.S.C. §§ 1301(a)(13) and (a)(14) (definitions of "contributing sponsor" and "controlled group").

[4] PBGC has issued proposed guidance: (1) interpreting the "established and maintained" language as "requir[ing] only that a plan be maintained by an employer—not both established and maintained—to come within the provisions of section 4062(e)"; and (2) limiting the scope of section 4062(e) to single-employer plans that are not multiple-employer plans. 75 Fed. Reg. 48283, 48284 and proposed § 4062.23(a)(1) (Aug. 10, 2010), available at http://www.pbgc.gov/Documents/2010-19627.pdf. For a detailed summary and analysis of 4062(e), *see* "Stealth Liability Lurks for Employers with Ongoing Pension Plans who Downsize or Sell Businesses" by Harold J. Ashner, Pension & Benefits Daily, Bloomberg BNA (175 PBD, 9/13/10;

liability formula rule,[5] the amount of the liability equals the plan's underfunding (measured on a conservative PBGC plan termination basis as if the plan had terminated immediately after the cessation of operations) multiplied by the percentage reduction in active participants.

Although the applicable statutory provisions[6] call for the liability to be satisfied through an escrow payment (or, if PBGC so requires, the purchase of a bond in an amount not exceeding 150 percent of the liability) to provide protection in case the plan is terminated in a distress or involuntary termination within the next five years, PBGC has generally attempted to negotiate alternative ways of satisfying the liability, most often with an employer commitment to make additional contributions to the plan that total the 4062(e) liability amount over a period of years.

The liability that arises in connection with a 4062(e) event can be surprisingly large. Consider, for example, a legacy plan with 50 active participants who all work at one facility, but with thousands of retirees and deferred vested participants. Assume that the plan is well funded or even overfunded on an ongoing funding basis, but underfunded by $250 million (based primarily on liabilities for inactive participants) on a PBGC plan termination basis, and that the employer, with a workforce of 50,000 employees on a controlled-group-wide basis, ceases operations at that facility and, as a result, separates all 50 active participants. Under PBGC's liability formula, the 4062(e) liability amount would be $250 million—$5 million for each of the 50 affected active participants.

## A Growing Controversy

Section 4062(e) has been law since ERISA's enactment on Sept. 4, 1974, but was essentially dormant for more than 30 years. Since 2006, however, it has been a centerpiece of PBGC's enforcement efforts. A brief chronology follows.

**Sept. 4, 1974, to July 16, 2006.** Section 4062(e) was rarely enforced by PBGC, largely because the statute did not provide clear rules as to the methodology for calculating the amount of the liability.

**July 17, 2006.** Relying on Section 4063(b) of ERISA,[7] which empowers PBGC to determine liability ''on any other equitable basis prescribed by the corporation in regulations,'' PBGC adopted a 4062(e) liability formula rule, which was effective on July 17, 2006.[8] As noted above, the regulatory formula provides that 4062(e) liability equals the amount of the plan's underfunding (using PBGC plan termination assumptions) multiplied by the active headcount reduction percentage. After promulgating the rule, PBGC stepped up its 4062(e) enforcement efforts.

**Aug. 10, 2010.** PBGC published a proposed rule addressing the circumstances in which 4062(e) could arise.[9] The proposal took expansive interpretative positions. For example, under the proposed rule, 4062(e) liability could be triggered based on:

- a going-concern asset sale, where operations and employment are discontinued with the seller but continue seamlessly with the buyer;
- the cessation of only one of multiple operations at a facility with all other operations continuing at full strength;
- the transfer of an operation from one facility to another facility of the same employer with no reduction in the number of employees or the overall level of operations; or
- a temporary cessation of operations at a facility, for example for maintenance or repair purposes, that continued for more than 30 days.[10]

**October—November 2010.** Public comments[11] strongly objected to the expansive interpretations reflected in PBGC's proposed rule.

**April 1, 2011.** PBGC announced, in response to the President's Executive Order 13563 on ''Improving Regulation and Regulatory Review,''[12] that it was undertaking a review of its regulations ''to make PBGC's regulatory program both more effective and less burdensome,'' and solicited public comments.[13]

**May 27, 2011.** PBGC issued its ''Preliminary Plan for Regulatory Review,'' which stated that ''[i]n light of industry comments, PBGC will . . . reconsider its 2010 proposed rule that would provide guidance on the applicability and enforcement of ERISA section 4062(e).''[14]

**Aug. 8, 2011.** The internal PBGC Appeals Board issued its first decision regarding 4062(e) liability, reducing the amount of the asserted liability by about 2 per-

37 BPR 2044, 9/14/10), at http://www.keightleyashner.com/publications/091410-BNA_Stealth.pdf.

[5] 29 CFR § 4062.8(a).

[6] ERISA Sections 4062(e) and 4063, 29 U.S.C. §§ 1362(e), 1363.

[7] 29 U.S.C. § 1363(b).

[8] 29 CFR § 4062.8; *see also* 71 Fed. Reg. 34819 (final rule and preamble); 70 Fed. Reg. 9258, 9259 (Feb. 25, 2005) (proposed rule and preamble, including discussion of the difficulty of applying the 4063 liability formula in a 4062(e) context); for a summary and analysis of the final rule, *see* ''PBGC's Final Rule on Liability for Facility Shutdowns Affects Downsizing Employers'' by Harold J. Ashner, Pension & Benefits Daily, Bloomberg BNA (121 PBD, 6/23/06; 33 BPR 1546, 6/27/06), at http://www.keightleyashner.com/publications/BNA_FinalRule062706.pdf; for a summary and analysis of the proposed rule, *see* ''PBGC Proposes Alternative Liability Calculation for Facility Shutdowns'' by Harold J. Ashner, Pension & Benefits Daily, Bloomberg BNA (39 PBD, 3/1/05; 32 BPR 575, 3/8/05), at http://www.keightleyashner.com/publications/4062e_reg.pdf.

[9] The 2010 proposed rule, published at 75 Fed. Reg. 48283 (Aug. 10, 2010), is available at http://www.pbgc.gov/Documents/2010-19627.pdf.

[10] For a summary and analysis of the 2010 proposed rule, *see* ''Stealth Liability Lurks for Employers with Ongoing Pension Plans who Downsize or Sell Businesses'' by Harold J. Ashner, Pension & Benefits Daily, Bloomberg BNA (175 PBD, 9/13/10; 37 BPR 2044, 9/14/10), at http://www.keightleyashner.com/publications/091410-BNA_Stealth.pdf.

[11] The public comments on the 2010 proposed rule are available at http://www.pbgc.gov/Documents/SubstantialCessationofOperationsComments(11).pdf.

[12] *See* http://www.gpo.gov/fdsys/pkg/FR-2011-01-21/pdf/2011-1385.pdf.

[13] 76 Fed. Reg. 18134 (April 1, 2011).

[14] *See* http://www.whitehouse.gov/files/documents/2011-regulatory-action-plans/PensionBenefitGuarantyCorporationPreliminaryRegulatoryReformPlan.pdf.

  

cent but otherwise upholding the agency's initial liability determination.[15]

**Aug. 23, 2011.** PBGC issued its "Plan for Regulatory Review," which reiterated that PBGC would reconsider its proposed 4062(e) rule.[16]

**Dec. 16, 2011.** Seven trade associations—the American Benefits Council, the ASPPA College of Pension Actuaries, the Committee on Investment of Employee Benefit Assets, the ERISA Industry Committee, the Financial Services Roundtable, the National Association of Manufacturers, and the U.S. Chamber of Congress—sent a joint letter to the PBGC Director expressing concern "that PBGC personnel, in communicating with plan sponsors, are referring to the [August 10, 2010] proposed regulations as current law, and enforcing them as such . . . . "[17] The letter requested, *inter alia*, that PBGC suspend all enforcement actions based on the proposed regulations.

**Feb. 2, 2012.** PBGC Director Joshua Gotbaum, in testimony before the Health, Employment, Labor and Pensions Subcommittee, House Committee on Education and the Workforce, stated that ". . . PBGC is . . . being more responsive to companies and plans in enforcing ERISA section 4062(e) . . . In light of comments, the agency plans to issue a re-proposed regulation on 4062(e). We have also begun to consider changes in how resources are directed within the 4062(e) enforcement program, in order to focus on the real threats to the retirement security of people in traditional pension plans."[18]

**Feb. 16, 2012.** Congressman Richard E. Neal (D-MA), Ranking Member of the Select Revenue Measures Subcommittee of the House Ways and Means Committee, introduced H.R. 4050, the Retirement Plan Simplification and Enhancement Act of 2012,[19] which would have significantly limited the scope of 4062(e) by providing generally that an employer would not be treated as having a 4062(e) cessation of operations unless:

(A) all operations at a facility in a location were ceased and –

(i) such cessation is reasonably expected to be permanent,

(ii) no portion of such operations is moved to another facility at a different location,

(iii) no portion of such operations is assumed or otherwise transferred to another employer, and

(iv) no other operations are reasonably expected to be maintained at such facility, and

(B) as a result of the cessation, more than 20 percent of the employees of the employer (determined on an aggregated controlled group basis) have a termination of employment that is reasonably expected to be permanent.

The Neal bill also would have significantly limited PBGC's 4062(e) enforcement discretion: although the bill would have applied only as of the date of enactment, rather than as of a retroactive date, it also provided that, as of the date of enactment, PBGC "shall not take any enforcement, administrative, or other actions pursuant to section 4062(e) that are inconsistent with [the requirement that there be a complete cessation of operations, as defined under (A), above], without regard to whether such actions relate to a cessation or other event that occurs before or after the date of enactment."

**Nov. 2, 2012.** PBGC announced that it was implementing a pilot program regarding enforcement of downsizing liability.[20] Under the pilot program, PBGC said, it would generally not enforce 4062(e) liability if a company was "financially sound" or "creditworthy," provided that there were no "other indicators of financial weakness" or "other risks." However, PBGC cautioned that "[i]f the company is no longer creditworthy during the five-year enforcement period, PBGC will enforce the 4062(e) liability," and noted that it "may periodically request additional information from the company to confirm its continued qualification as creditworthy." PBGC also said that it would not enforce 4062(e) liability in small plan situations based on a 100-participant threshold.[21]

Although PBGC did not state any intention to change any of the specific 4062(e) interpretations reflected in its 2010 proposed rule, the agency did say that it would be "using this pilot program to help [it] decide what changes to make in [its] proposed regulation."

**May 22, 2013.** Congressman Neal introduced H.R. 2117, the Retirement Plan Simplification and Enhancement Act of 2013.[22] The provisions in H.R. 2117 were substantively very similar to those in H.R. 4050, which Congressman Neal had introduced in 2012.

**Dec. 31, 2013.** The internal PBGC Appeals Board issued its second and third decisions; both decisions affirmed the agency's imposition of 4062(e) liability.[23]

**January—February 2014.** PBGC began to assert the position that liens for 4062(e) liability may arise on all of an employer's property and that PBGC may perfect those liens.[24]

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[15] *See* http://www.pbgc.gov/Documents/apbletter/Decision--Bendix-Commercial-2011-08-08.pdf; for a description and analysis of the Appeals Board's decision, *see* http://www.keightleyashner.com/alert083011.htm.

[16] *See* http://www.pbgc.gov/documents/plan-for-regulatory-review.pdf. *See also* http://www.pbgc.gov/news/press/releases/pr11-54.html.

[17] *See* http://www.americanbenefitscouncil.org/documents/4062e_group_letter1211.pdf.

[18] *See* http://www.pbgc.gov/news/testimony/page/tm020212.html.

[19] *See* https://www.govtrack.us/congress/bills/112/hr4050.

[20] *See* http://www.pbgc.gov/news/press/releases/pr12-32.html; http://www.pbgc.gov/about/faq/pg/frequently-asked-questions-4062.html; http://www.pbgc.gov/Documents/4062(e)-enforcement-of-guidelines.pdf.

[21] For a summary and analysis of the pilot program, *see* "PBGC Announces 4062(e) Enforcement Pilot Program: Who Will Qualify for Relief?" by Harold J. Ashner and Deborah G. West, Pension & Benefits Daily, Bloomberg BNA (217 PBD, 11/9/12; 39 BPR 2173, 11/13/12), at http://www.keightleyashner.com/publications/110912-BNA-4062e.pdf; *see also* "PBGC Changes 4062(e) Enforcement; Financially Sound Plans Exempt, Agency Says," Pension & Benefits Daily, Bloomberg BNA (213 PBD, 11/5/12; 39 BPR 2080, 11/6/12) at http://www.keightleyashner.com/publications/110612-PBGC-PilotProgram.pdf.

[22] *See* https://www.govtrack.us/congress/bills/113/hr2117.

[23] *See* http://www.pbgc.gov/documents/apbletter/Decision--Home-Meridian-Plan-2013-12-31.pdf; http://www.pbgc.gov/documents/apbletter/Decision--Munksjo-Plan-2013-12-31.pdf.

[24] *See* http://www.keightleyashner.com/alert052814.htm; http://www.americanbar.org/content/dam/aba/events/employee_benefits/2014_pbgc_qa.authcheckdam.pdf (*see* PBGC staff response to question 17 regarding whether 4068 liens may arise in connection with 4062(e) liability).

**Jan. 30, 2014.** Senator Tom Harkin (D-IA), the Chairman of the Senate Health, Education, Labor and Pensions Committee, introduced S. 1979, which provided for a two-year moratorium on any PBGC 4062(e) enforcement actions, during which time the Government Accountability Office would be directed ''to study the effectiveness, fairness, and utility of such shutdown liability requirements.''[25]

**June 3, 2014.** In a letter[26] to the PBGC Board of Directors, the American Benefits Council, the ASPPA College of Pension Actuaries, the Committee on Benefits Finance of Financial Executives International, and The Committee on Investment of Employee Benefit Assets, stated that PBGC's 4062(e) enforcement actions ''reflects a policy position that in our view is not consistent with the law and that is adversely affecting critical business transactions needed for companies to recover'' and that resulted in ''unnecessary harms to plan sponsors.'' The letter also stated:

- Despite PBGC's announcement that it is reconsidering its expansive 2010 proposed 4062(e) regulations, PBGC is taking an enforcement position that is almost identical to the proposed regulations.

- The imposition of 4062(e) liability diverts assets away from a company's business, which has very adverse effects on companies, business recovery, and jobs.

- The imposition of 4062(e) liability harms plan participants by driving companies to exit the pension system.

- PBGC's practice of negotiating with employers to increase pension plan funding results in large and disproportional funding that is in substance an end run around Congressional funding rules—an end run that is applied only to those companies that happen to engage in business transactions that are captured by PBGC's expansive and inappropriate approach to 4062(e), creating substantial unfairness as compared to their competitors.

- PBGC's decision to exempt ''creditworthy'' companies from its enforcement effort does not adequately address companies' concerns: for example, no company, even one that is financially strong today, wants to face a future where if the company confronts financial challenges, it may suddenly have a large PBGC liability for a previous business transaction, nor does any company want to be severely limited in its ability to engage in helpful future business transactions. Moreover, the imposition of 4062(e) liabilities on a company facing business challenges may severely harm the company's recovery, which is in no one's interest, including PBGC.

**June 19, 2014.** Senator Harkin introduced S. 2511, a bill that would amend ERISA to clarify the definition of substantial definition of operations for 4062(e) purposes.[27]

**July 8, 2014.** PBGC announced a moratorium on its enforcement of Section 4062(e). The moratorium was immediately effective and continues until Dec. 31, 2014.

**July 23, 2014.** The HELP Committee approved a modified version of S. 2511 by a bipartisan voice vote.[28]

## PBGC Enforcement Moratorium

Although employers must continue to comply with the statutory and regulatory reporting requirements that pertain to potential 4062(e) events,[29] the moratorium provides employers with the assurance that PBGC will not enforce 4062(e) cases for the balance of calendar year 2014. Beyond that, however, there is little certainty.

In its moratorium announcement, PBGC said that the moratorium would ''enable PBGC to ensure that its efforts are targeted to cases where pensions are genuinely at risk.''[30] PBGC also said that the six-month period would ''allow us to work with the business community, labor, and other stakeholders.'' Accordingly, one can hope that, by the time the moratorium ends, PBGC will have modified its 4062(e) enforcement approach to be more responsive to the concerns expressed by Congress, employers, and trade groups—whether independently or in response to (or in conjunction with) legislative change.

As discussed in detail below, 4062(e) reform legislation is now being seriously considered; if legislation is enacted, it will likely alter the statutory and enforcement landscape significantly.

Finally, it is possible that, come Jan. 1, 2015, the currently existing statutory and regulatory provisions, as well as PBGC's current enforcement approach, will remain unchanged, and PBGC will simply recommence its pursuit of currently pending 4062(e) cases—with one significant exception. Section 4062(e) liabilty is abated if the plan is not terminated in a distress or involuntary termination within five years; any escrow is returned to the employer without interest and any bond is cancelled.[31] Thus, as a result of the statutory five-year ''shelf life,'' a 4062(e) claim against an employer who has neither reached a settlement with PBGC nor agreed to toll the statutory five-year period will be moot if the five-year liability period has run by the end of the moratorium period; other such employers will be almost six months closer to the expiration of the five-year liability period.

Thus, employers should keep in mind that business decisions made or implemented during the moratorium period could result in PBGC's assertion of new 4062(e) claims, whether under current law and PBGC enforcement policy, or under changed legal or enforcement standards. Consequently, an employer is faced with the challenging imperative of considering the 4062(e) implications of potential downsizing decisions without knowing what the legislative, regulatory, or enforcement policy environment will be after the moratorium ends.

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[25] *See* https://beta.congress.gov/bill/113th-congress/senate-bill/1979.

[26] *See* http://www.americanbenefitscouncil.org/documents2014/4062e_groupletter072314.pdf.

[27] *See* https://beta.congress.gov/bill/113th-congress/senate-bill/2511.

[28] *See* https://beta.congress.gov/bill/113th-congress/senate-bill/2511/actions.

[29] *See* http://www.pbgc.gov/news/press/releases/pr14-09.html; *see* 29 U.S.C. § 1363(a), http://www.pbgc.gov/prac/reporting-and-disclosure/section-4063-notices.html.

[30] *See* http://www.pbgc.gov/news/press/releases/pr14-09.html.

[31] *See* ERISA Sections 4062(e) and 4063(c)(2), 29 U.S.C. §§ 1362(e), 1363(c)(2).

## On the Horizon: Possible Legislative Changes

With the Senate HELP Committee's July 23, 2014, bipartisan voice vote approval of a modified version of S. 2511,[32] the likelihood of legislative change during the moratorium period appears to have increased. The bill has not yet gone to the full Senate, but that may happen in the near future; it will likely undergo further changes and clarifications—perhaps significant ones—as it moves forward.

Of course, there is no guarantee that S. 2511—or any other 4062(e) legislation—will pass, and no certainty as to what provisions would be included in any enacted legislation. Nonetheless, a general familiarity with key aspects of S. 2511 may assist an employer in evaluating potential business transactions[33] that may have 4062(e) implications, whether under the current statutory, regulatory, and enforcement landscape or under one that has changed, perhaps significantly.

In general terms, as of this writing, the bill would change the definition of a 4062(e) event, and would provide employers with the right to elect to satisfy the liability in a different way.

**Change In Definition Of 4062(e) Event.** Under the current version of S. 2511, a 4062(e) event (referred to as a ''substantial cessation of operations'') would occur with respect to any PBGC-covered single-employer plan established and maintained by an employer covering participants at a facility if: (1) the employer permanently ceases operations at the facility; and (2) as a result, there is a workforce reduction of more than 15 percent of all eligible employees at all facilities in the contributing sponsor's controlled group, determined immediately before the date of the employer's decision to implement the cessation.

The term ''workforce reduction'' means the number of eligible employees at a facility who are separated from employment by reason of the permanent cessation of operations of the employer at the facility. An ''eligible employee'' is one eligible to participate in any employee pension benefit plan (whether defined benefit or defined contribution) as defined in ERISA Section 3(2) established and maintained by the employer.[34]

**Rules For Excluding Eligible Employees.** The bill provides the following rules for excluding eligible employees from the workforce reduction numerator in determining whether the 15 percent threshold has been crossed:

- An eligible employee separated from employment at a facility is *not* taken into account in computing a workforce reduction if, within a reasonable period of time, the employee is replaced by the employer, at the same or another facility in the United States, by an employee who is a citizen or resident of the United States.

- In the case of a sale or other disposition of the assets or stock of a contributing sponsor (or any member of the same controlled group as such a sponsor) of the plan relating to operations at a facility, an eligible employee is *not* taken into account if the acquiring person maintains the single employer plan of the predecessor employer that includes assets and liabilities attributable to the accrued benefit of the employee at the time of the sale or disposition and *either:*
  - the eligible employee is separated from employment at the facility but, within a reasonable period of time, is replaced by the acquiring person by an employee who is a citizen or resident of the United States; *or*
  - the eligible employee continues to be employed at the facility by the acquiring person.

**Three-Year Lookback.** There is a three-year lookback for purposes of determining whether the 15 percent threshold is crossed; the proposed bill provides that the workforce reduction with respect to any cessation of operations is determined by taking into account (subject to the two rules described above) the separation from employment of any eligible employees at the facility occurring during the three-year period preceding such cessation.

**New Option For Satisfying Liability.** The bill would also provide employers with the option of electing an alternative method of satisfying the employer's 4062(e) liability with respect to a plan. It is important to keep in mind that a cessation of operations at a facility that results in a workforce reduction that crosses the 15 percent threshold under the bill may trigger 4062(e) liability with respect to more than one plan. If that occurred, it would be necessary to analyze each plan to determine whether the alternative method for satisfying liability should be elected with respect to that plan.

Under the alternative method, the employer would make additional contributions to the plan for seven years (in excess of the minimum required contribution under Section 430 of the Internal Revenue Code); the extra contributions could not be satisfied by—or used as—a prefunding balance. The annual additional contribution amount would be determined by multiplying:

- One-seventh of the plan's unfunded vested benefits determined under variable-rate premium rules for the plan year before the year the event occurred; *by*

- A ''reduction fraction'' equal to the number of plan participants counted in the workforce reduction (using the same rules described above that are applicable to the determination of whether the 15 percent liability trigger is met) divided by the total number of participants working at the facility who had accrued benefits in the plan immediately before the employer decided to cease operations there.

The seven-year period would begin with the plan year in which the cessation occurred, and the additional contribution would be paid not later than the earlier of:

- the due date for the minimum required contribution for the year; *or*

- in the case of the first such contribution, the date that is one year after the date on which the employer

[32] *See* https://beta.congress.gov/bill/113th-congress/senate-bill/2511/actions. The draft text of the amended S. 2511 is at http://op.bna.com/pen.nsf/r?Open=krkl-9mcsd6.

[33] This article uses the term ''transactions'' inclusively to encompass *all* significant business events, whether or not they involve an unrelated person. Thus, a ''transaction'' includes an employer's implementation of its decision to cease operations at a facility as well as a stock or asset sale to an unrelated person.

[34] This article assumes that PBGC would interpret the ''established and maintained'' language in this context in the same way it has proposed to interpret that language in the context of existing 4062(e), *i.e.*, as meaning just ''maintained.'' *See* footnote 4, *supra*.

notifies PBGC of the substantial cessation of operations or the date PBGC determines that a substantial cessation of operations has occurred, and in the case of subsequent contributions, the same date in each succeeding year.

For any plan year, the additional required contribution could not exceed the excess, if any, of (a) 25 percent of the difference between the market value of the assets of the plan and the funding target of the plan (both as determined under variable-rate premium rules) for the preceding plan year, over (b) the minimum required contribution for the plan (as determined under statutory funding rules) for the current plan year.

If an employer fails to pay the additional contribution in the full amount for any year in the seven-year period by the due date for that payment, all unpaid additional contributions required to be paid by the employer for the entire seven-year period would become due and payable as of the same date as the missed contribution. The bill also provides that PBGC could waive or settle the accelerated liability in its discretion.

An employer's obligation to make the additional seven annual contributions would cease with respect to the first plan year for which the ratio of the market value of the plan assets to the funding target of the plan for the plan year is 90 percent or greater and any subsequent plan year in the seven-year period. In addition, the obligation would be permanently waived with respect to any plan year for which the Secretary of the Treasury issued a funding waiver.

The obligation would exist only under Title IV of ERISA, and not under the Internal Revenue Code. PBGC would be empowered to file an action in the appropriate United States district court to compel an employer making the election to pay the additional contributions.

As discussed in more detail below, the bill includes a transition rule providing that an employer that had a 4062(e) cessation of operations event before June 1, 2014, shall be permitted to elect to satisfy the liability via the alternative method under certain circumstances.

**Exemptions.** A plan would be exempt from 4062(e) liability if, for the plan year preceding the plan year in which the cessation occurred, *either:*

- there were fewer than 100 participants with accrued benefits under the plan as of the valuation date for the plan year, *or*

- the ratio of the market value of the assets of the plan to the funding target of the plan for the plan year was 90 percent or greater.

**Effective Date and PBGC Enforcement Restrictions.** In its current form, the bill provides that the new provisions would apply to cessations of operations or other events at a facility that occur on or after June 1, 2014, subject to three important exceptions:

- Employers that had a cessation of operations before June 1, 2014 (as determined under Section 4062(e) as in effect on such date), but did not enter into an arrangement with PBGC to satisfy the liability before the date of enactment, would be permitted to make the election to satisfy the liability by using the alternative method (described above) as if the cessation had occurred on June 1, 2014. The election would have to be made not later than 30 days after PBGC notified the employer, on or after the date of the bill's enactment, that PBGC had determined that a substantial cessation of operations (as defined under the new statutory rules) had occurred.

- PBGC would be prohibited from taking actions inconsistent with the new statutory rules with respect to pending cases, without regard to whether the cessation or other event occurred before, on, or after the date of the bill's enactment (except for cases regarding which settlement agreements were in place before June 1, 2014).

- PBGC would be prohibited from initiating a new enforcement action that is inconsistent with its enforcement policy as in effect on June 1, 2014.

## The Proposed Bill and Current Law

**Liability Trigger.** Under both current law and the proposed bill, the liability is triggered when an employer ceases operations at a facility and, as a result, a specified percentage of employees is separated from employment. Under current law, the requisite percentage is *more than 20 percent* of the total number of employees *who are participants in one PBGC-covered single-employer plan*. Under the proposed bill, the requisite percentage is *more than 15 percent* of the total number of ''eligible employees'' at all facilities of the employer. An eligible employee is one who is *eligible to participate in an employee pension benefit plan* established and maintained by the employer.

The new liability trigger would ensure that the event triggering 4062(e) liability is significant relative to the total number of employees in the contributing sponsor's controlled group. By contrast, under current law, it is possible for a transaction that affects a very small portion of the controlled group work force to trigger a very large liability. For example, an employer may decide to shut down a money-losing facility where less than 1 percent of the employer's employees work. If all active plan participants in one PBGC-covered plan work at that facility and are separated as a result of the shutdown, there would be a 4062(e) liability equal to 100 percent of the plan underfunding on a plan termination basis. Where, as is common, the plan underfunding includes large legacy liabilities, the liability can be massive. The bill's ''right-sizing'' of the liability trigger percentage is one of its most welcome reforms.

At the same time, it is important to recognize that under the proposed bill, 4062(e) liability could be triggered with respect to a plan regardless of how many active plan participants at the facility separate from employment as a result of a cessation of operations that crossed over the 15 percent workforce reduction threshold. Again, under current law, liability is not triggered unless more than 20 percent of active plan participants are separated from employment as a result of the cessation.

Under the proposed bill, both the numerator and the denominator used to determine the 15 percent threshold would have a broader sweep than that under current law by including not only employees who are participants in a PBGC-covered plan, but also *all* employees of the Title IV employer (*i.e.*, the contributing sponsor and all members of its controlled group) who are eligible to participate in any employee pension benefit plan established and maintained by the employer—whether a defined benefit plan or a defined contribution plan. It is important to note that both the numerator and the denominator may include employees who are *eligible* to participate in, for example, a 401(k) plan, whether or not they choose to do so. For an employer whose retirement plans cover all full-time (and no part-time) employees, the bill's ''eligible employees'' formulation is, in essence, a proxy for an employer's full-time domestic workforce.

Significantly, under the proposed bill in its current form, the numerator (but not necessarily the denominator) would include eligible employees at the facility who separated from employment during the three-year period preceding the cessation date, whether or not their separation was caused by or otherwise related to the cessation. As discussed below, the three-year aggregation provision raises a number of issues that may be addressed by clarifying changes as the bill moves forward.

In one respect, the numerator under the bill is narrower than that under current law, because it is only employees *at the facility* where operations ceased who may be counted in determining whether there has been a greater than 15 percent workforce reduction that triggers 4062(e) liability. Under PBGC's interpretation of current law, if the cessation of operations at a facility results in the separation from employment of plan participants at other, ongoing facilities, those participants must be included in the numerator;[35] because the denominator includes all active plan participants, they are included in the denominator as well.

**New Alternative Liability Method.** Under both current law and the proposed bill, the amount of the liability is a portion (which may be 100 percent) of the plan's underfunding, as measured on a conservative PBGC plan termination basis. As noted above, the liability may be satisfied via the provision of an escrow or (if PBGC so requires) a bond in an amount not exceeding 150 percent of the liability.[36]

As discussed above, the proposed bill would provide employers with the right to elect an alternative method for measuring and satisfying the liability: the employer could make annual additional contributions for a seven-year period that would fund a specified percentage of the total plan underfunding, as measured under variable-rate premium rules (which is likely to be significantly less than underfunding measured on a termination basis).

As also discussed above, if a plan is at the 90 percent level for the plan year preceding the year in which a substantial cessation of operations occurred, the plan would be exempt from 4062(e) liability with respect to that cessation. Achieving the 90 percent funding level for any later year in the seven-year payment period continues to have significant favorable consequences if the employer elects the alternative method: once a plan achieves that funding level, the employer's obligation to make the additional funding contributions under the alternative method would cease.

By way of illustration, an employer whose plan is at the 90 percent level for the plan year in which a 4062(e) event occurred could elect the alternative method and be immediately released from the seven-year funding obligation (and from 4062(e) liability with respect to the plan) without making any liability payments; an employer whose plan achieved the 90 percent level in the year following the year in which the event occurred would be released from liability after making one of the seven annual additional contributions. These provisions provide additional incentives for an employer to achieve a 90 percent funding level.

Even where the plan has not yet achieved a 90 percent funding level, as discussed in detail earlier, the bill provides that the annual additional required contribution cannot exceed 25 percent of the plan's unfunded vested benefits determined under variable-rate premium rules for the prior year minus the minimum required contribution for the plan year. The cap is increasingly likely to be helpful as the plan's funding percentage improves over time.

The provision of an option to elect to satisfy 4062(e) liability in a way that does not require a negotiated agreement (or judicial resolution) would enable an employer to resolve 4062(e) liability promptly and in a way that is consistent with the employer's business needs and strategies—another welcome change from current law.

It is important to be aware that the application of the rules governing the proposed bill's elective method for satisfying 4062(e) liability may yield unexpected results in particular cases. On the one hand, as noted above, the total plan underfunding, which would be measured on a variable-rate premium basis, may be significantly less than that measured on a termination basis. On the other hand, the headcount ''reduction fraction'' under the elective method may be surprisingly large.

Consider a permanent cessation of operations at a facility that results in the separation from employment of all eligible employees at the facility, who constitute 16 percent of the total number of eligible employees in the controlled group. Prior to the cessation, there was a total of 100 active participants in the PBGC-covered plan maintained by the employer. Four of the 100 active participants worked at the facility experiencing the cessation; all four separated from employment by reason of the cessation. The remaining 96 actives continued to work at other facilities and were unaffected by the cessation of operations.

No 4062(e) liability would arise under current law, which requires that more than 20 percent of the total number of active plan participants must separate from employment; here only four percent of the actives have separated. Under the proposed bill, however, there would be a substantial cessation of operations because the 15 percent workforce reduction liability threshhold has been crossed. And, because four out of four active plan participants at the facility separated from employment, the headcount ''reduction fraction'' for purposes of the alternative liability method would be 100 percent—notwithstanding the fact that 96 percent of the active plan participants were unaffected by the facility shutdown.

It is worth repeating that, as under current law, the cessation of operations at a single facility could trigger 4062(e) liability with respect to more than one PBGC-covered plan under the bill's provisions. If a 4062(e) event occurred under the bill's provisions, it would not be surprising if liability arose with respect to a plan, for example, in which 25 percent of active participants

[35] *See* 75 Fed. Reg. 48283, 48287, 48292, proposed 29 CFR § 4062.28(b)(3).

[36] 29 U.S.C. § 1363(b), (c).

separated from employment. But the fact that liability could also arise with respect to a second plan in which only 5 percent of the active plan participants separated from employment could well catch an employer by surprise.

The bill's provisions regarding the alternative method present a number of timing issues that could prove to be problematic, particularly in cases in which the employer does not believe that a 4062(e) event has occurred. If, for example, PBGC issues a liability determination two or three years after the alleged cessation of operations has occurred, the employer will have missed the deadline for making the contribution, and all seven years of payments would become immediately past due.[37] The same problem arises with respect to an employer who meets PBGC's financial soundness standards under its 4062(e) enforcement policy for the first few years after the cessation of operations, but then falls below those standards before the end of the five-year period. Moreover, even assuming that PBGC timely issues an initial liability determination, the employer may wish to contest the determination before making an election to satisfy the disputed liability. Hopefully these issues will be clarified as the bill moves forward.

**PBGC Positions Foreclosed.** The proposed bill would provide new statutory rules that would foreclose certain PBGC interpretative positions. Two illustrative examples follow.

First, under current law, if an employer ceases operations at a facility in any location, and, ''*as a result of such cessation of operations*,'' more than 20 percent of the total number of active plan participants are separated from employment, there is a 4062(e) event.[38] PBGC has taken the position that an employee's separation may be the result of the cessation of operations at a facility even if the separated employee's employment was at another facility.[39]

Under the proposed bill, there is a 4062(e) event only if there is a substantial cessation of operations at a facility which results in a ''workforce reduction of a number of eligible employees *at the facility* equivalent to more than 15 percent of the number of all eligible employees at all facilities of of the employer . . . . '' The bill's explicit language thus would appear to foreclose a position that job losses at other facilities can be taken into account in determining whether the requisite percentage of employees has separated from employment in connection with the cessation of operations at the facility.

Second, PBGC has taken the position that 4062(e) liability can be triggered even if the cessation of operations is temporary.[40] It appears that such a position would be foreclosed if the proposed bill becomes law: the bill specifies that the ''[t]erm 'substantial cessation of operations' means a *permanent* cessation of operations at a facility. . . . ''

**Gray Areas Remaining.** Under the proposed bill, some of the gray areas that exist under current law will remain gray areas. Among them are the following:

- What constitutes a ''facility?''
- Can two or more geographically proximate buildings at which the same or related ''operations'' are conducted constitute a ''facility''?
- Can there be two ''facilities'' within a single building?
- Can the cessation of only one set of ''operations'' be enough to trigger liability where other ''operations'' continue at the same facility? If so, what what constitutes ''operations'' that are sufficiently distinct from other ''operations'' at the same facility?
- Must the ''cessation'' of the operations (or of all of the operations) at the facility be a complete cessation, without regard to the completion of any work in progress?
- What is the date of a ''cessation'' when it occurs in two or three stages, or gradually over an extended period of time?
- What about employees who separate on or shortly after the cessation date for reasons not clearly tied to the cessation (including, for example, normal attrition, retirement, or death)?
- At what point is an employee considered separated from employment? What about, for example, employees who are on layoff and/or subject to recall? What about employees on long-term disability? Does it matter how long they have been on disability? Does it matter what the expectations are regarding the employee's return to work?

**Unanswered Questions in Bill.** In addition, there are, unsurprisingly, a number of unanswered questions regarding the bill's provisions; clarifying and other changes likely will be made to the proposed bill as it moves forward.

For example, the bill specifies that the term ''workforce reduction'' means ''the number of eligible employees at a facility who are separated from employment *by reason of* the permanent cessation of operations of the employer at the facility.'' However, the bill's aggregation provision—which provides that separations occurring during the three-year period *preceding* the cessation of operations are taken into account in determining the workforce reduction—does *not* require that there be a causal link between the separations and the cessation. Thus, employees who separated from employment on or after the cessation date will be counted only if they separated because of the cessation, but employees who

[37] In the three 4062(e) liability cases decided by the PBGC Appeals Board to date, two of the three initial liability determinations were issued more than three and a half years after the alleged cessation of operations; the third was issued more than two years after the alleged cessation. *See* http://www.pbgc.gov/Documents/apbletter/Decision--Bendix-Commercial-2011-08-08.pdf; http://www.pbgc.gov/documents/apbletter/Decision--Home-Meridian-Plan-2013-12-31.pdf; and http://www.pbgc.gov/documents/apbletter/Decision--Munksjo-Plan-2013-12-31.pdf.

[38] 29 U.S.C. § 1362(e) (emphasis added to quoted language).

[39] *See* 75 Fed. Reg. 48283, 48287.

[40] *See, e.g.*, 75 Fed. Reg. 48283, 48291, proposed 29 CFR § 4062.26(b)(2) (in the case of certain involuntary cessations, the employer is considered to have ceased an operation no later than the date that is 30 days after the discontinuance of activity, regardless of whether activities later resume).

separated within the three-year period prior to the cessation date will be included without regard to causality. The absence of a causality requirement in the three-year aggregation provision may lead to both uncertainty and unintended results. For example, an employee who retired as planned on his 65th birthday would not be included in the count if that date occurred on or after the cessation date, but the same employee *would* be included if the date occurred prior to the cessation date.

The three-year aggregration provision may also need to be clarified to ensure that there is a logical correlation between the numerator (which would be measured over a three-year period) and the denominator (which would be measured immediately before the date of the employer's decision to implement the cessation). For example, where there is a temporary spike in employment during the 3-year period, it may not be appropriate to include separations that occurred when employment returned to normal levels. Moreover, clarification that separations that have already given rise to liability should not be counted would appear to be appropriate to prevent double counting.

A number of questions are raised by the bill's provisions that a separated employee who has been ''replaced'' is not counted in determining the workforce reduction, including whether the new hire must perform exactly (or substantially) the same tasks as did the employee he or she ''replaced.''

A final example involves the bill's provisions regarding the sale or other disposition of the assets or stock of a contributing sponsor (or any member of the same controlled group as such a sponsor) of the plan relating to operations at a facility. The bill provides that eligible employees are not taken into account if they either continue to be employed at the facility by the acquiring person or are replaced by the acquiring person by an employee who is a citizen or resident of the United States *as long as the* acquiring person maintains the single employer plan of the predecessor employer that includes assets and liabilities attributable to the accrued benefit of the employee at the time of the sale or disposition. Thus, under the bill's current language, an eligible employee who continues in employment at the facility with (or whose U.S. citizen replacement is employed by) the acquiring person, but who is not a participant in any PBGC-covered single-employer plan (*e.g.*, an eligible employee covered only by a 401(k) plan) *is* taken into account *even if* the acquiring person maintains all of the seller's PBGC-covered single-employer plans after the sale. In addition, the bill's current language would appear to support a conclusion that the *entire plan* that was maintained by the predecessor employer must be assumed by the acquiring person, rather than, *e.g.*, just the portion of the plan representing the liabilities for employees who continue in employment with (or whose U.S. citizen replacements are employed by) the acquiring person. These results may not have been intended.

Finally, and as discussed above, the current bill would not alter the statutory provisions applicable to the determination of the amount of 4062(e) liability. But because those statutory provisions pertain to 4063 liability with respect to an employer's withdrawal from a multiple employer plan, they do not provide a workable formula for determining the amount of 4062(e) liability, which involves a single employer. Consequently, the liability amount currently is determined pursuant to PBGC's regulatory liability formula, 29 CFR § 4062.8.

PBGC's regulatory liability formula is based on the existing statutory language, which provides that the numerator for the 4062(e) liability trigger is determined by reference to the total number of plan participants who are separated from employment ''as a result of'' the cessation of operations. The bill would make it clear that only participants who work at the facility where operations ceased are included in the numerator. Consequently, if the bill is enacted, it is unclear whether PBGC could or would seek to apply the current formula—which is based on statutory language that would have been repealed and replaced—to cases arising after enactment, or whether PBGC might seek to change those rules in some manner.

**Impact on Existing Cases.** As noted above, the bill's general effective date is with respect to events occurring on or after June 1, 2014. In the case of an event that would trigger 4062(e) liability under the language of the bill but not under existing law, this could result in the liability being triggered retroactively. Hopefully the bill will be revised to avoid this result.

Of particular importance to employers with pending 4062(e) cases, the bill would direct PBGC not to take any enforcement, administrative, or other action that is inconsistent with the bill's provisions, without regard to whether the action relates to a cessation or other event that occurs before, on, or after the date of the enactment. The only exception is with respect to actions in connection with settlement agreements that were in place before June 1, 2014.

Thus, as a practical matter, the bill's provisions would be applicable to currently existing cases that were not settled before June 1, 2014. For example, assume that a cessation of operations that occurred on July 15, 2012, resulted in the separation from employment of more than 20 percent of active plan participants, thus triggering 4062(e) liability under current law. If the employer's workforce reduction was 15 percent or less of all eligible employees (as determined under the bill), PBGC would be precluded from taking any action to collect the 4062(e) liability that arose under prior law.

If, on the other hand, the July 15, 2012, cessation of operations resulted in the separation from employment of more than 20 percent of active plan participants *and* more than 15 percent of the employer's workforce, the cessation would be a 4062(e) event under the new provisions, and the employer could elect the alternative liability amount not later than 30 days after PBGC notifies the employer, on or after the date of the bill's enactment, that a 4062(e) event has occurred.

Moreover, the bill would preclude PBGC from initiating new 4062(e) enforcement actions that are inconsistent with its enforcement policy in effect on June 1, 2014. PBGC's enforcement guidelines provide that PBGC will not initiate enforcement of Section 4062(e) liability ''if and for so long as'' the employer is deemed financially sound, or with respect to small plans (based on a 100-participant threshold).[41]

[41] PBGC's 4062(e) enforcement guidelines, which were adopted in October 2012, are available at: http://www.pbgc.gov/Documents/4062(e)-enforcement-of-guidelines.pdf.

## Conclusion

Evaluating the 4062(e) implications of potential transactions that are under consideration in the current uncertain environment is challenging, yet it must be done. The most prudent approach may be to evaluate potential transactions under both current law *and* proposed S. 2511—while recognizing that the bill may not be enacted in its current form or at all. The ideal transaction would be one that effectively serves the employer's business needs and that would not trigger 4062(e) liability *either* under current law *or* under the proposed bill. An employer who considers the implications before selecting and implementing a business transaction may be able to take steps that would change the result.

While PBGC's 4062(e) enforcement moratorium provides something of a temporary respite, it remains important that employers plan effectively in connection with any possible 4062(e) event. In many cases, even with the current uncertainty, it may well be possible to structure the transaction so that the liability will not arise, or to take steps to minimize the amount of the liability. Where it appears that the liability likely will arise, it is important to take it into account as part of the planning stage, with a view toward ensuring that any liability and its resolution will fit within the employer's business plans.



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