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PBGC

Mediation of PBGC Disputes: A New and Welcome Option

BY HAROLD J. ASHNER AND DEBORAH WEST

On October 16, 2017, PBGC announced that it ''is beginning a pilot program that will offer mediation to plan sponsors to facilitate resolution in two key PBGC program areas.'' Under the new program, mediation will be available ''to ongoing plan sponsors as part of [PBGC's] Early Warning and Risk Mitigation Program and to former plan sponsors as part of resolving their pension liabilities following termination of underfunded pension plans.'' *See www.pbgc.gov/prac/other-guidance/pbgc-plan-sponsor-pilot-mediation-project.* Resolving disputes with PBGC in these two areas is often of critical importance to affected employers.

PBGC stated that the pilot program ''will allow parties to resolve cases with the assistance of a skilled, neutral and independent dispute resolution professional in a timely and cost-effective manner,'' and that mediation ''will be offered to eligible respondents and proceed purely on a voluntary basis.''

The pilot program is being implemented pursuant to an interagency agreement between PBGC and the Federal Mediation and Conciliation Service, which will provide the mediators. PBGC stated that it expects the pilot program to last for one year, and that it will thereafter evaluate the success of the program taking into account plan sponsor feedback.

In its announcement, PBGC stated that its goals for the pilot program are to resolve disputes early, to promote improved relations with stakeholders, to reduce the costs of protracted negotiations and other proceedings, and to make alternative dispute resolution (''ADR'') an integral part of the agency's dispute resolution process. Hopefully, PBGC will achieve these goals, continue to offer a mediation option, and expand its availability to cover other areas.

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This article provides a brief history of the background leading to the pilot mediation program, a description of the two categories of disputes that are eligible for the program, and a summary of the basic rules that apply to the program. Although PBGC's announcement refers repeatedly to the ''plan sponsor,'' this article assumes that PBGC's use of that term is shorthand for any or all of the entities that collectively constitute the ''employer'' standing behind a plan for purposes of Title IV of ERISA, *i.e.*, the contributing sponsor of the plan and all members of its controlled group.

Background Leading to Pilot Mediation Program

On April 12, 1999, PBGC announced its ''policy to use alternative dispute resolution for resolving disputes in a timely and cost-efficient manner,'' and observed that various forms of ADR, including mediation, ''often can provide faster, less expensive, and more effective resolution of disputes that arise with employees, contractors, the regulated community and others with whom the agency does business.'' 64 Fed. Reg. 17696. In practice, however, in the years following this announcement, there was relatively little use by PBGC of mediation and other forms of ADR in connection with disputes with employers.

In a May 8, 2013, meeting with representatives of the ABA's Joint Committee on Employee Benefits, PBGC staff stated that, although PBGC had used ADR in various contexts, including in the internal labor relations context, it had not done so in the Early Warning Program context. *See Q&A 33 at www.americanbar.org/content/dam/aba/events/employee_benefits/2013_pbgc_qa.authcheckdam.pdf.* The Participant and Plan Sponsor Advocate at PBGC stated in her 2014 Annual Report (available at www.pbgc.gov/oppsa) that ''outside of the internal labor and employment relations arena, PBGC has made little use of ADR in lieu of its adversarial ad-

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ministrative review and litigation approach, which can be costly both to PBGC and plan sponsors,'' and recommended that PBGC ''use ADR far more broadly in its dealings with sponsors.'' And in her 2016 Annual Report (also available at www.pbgc.gov/oppsa), the Advocate reiterated her recommendation that PBGC ''consider ADR as a faster and more cost effective solution for sponsors to resolve their disputes with [PBGC].''

The newly-announced mediation pilot program thus represents a significant change from PBGC's historical approach to ADR—a change that will likely be well-received by the employer community. As stated by Lynn Dudley, Senior Vice President, Global Retirement and Compensation Policy, for the American Benefits Council, ''[t]his is an excellent signal that PBGC is listening to plan sponsors and being creative to improve its programs and its relationships with sponsors.'' *See www.pbgc.gov/news/press/releases/pr17-07.*

Covered Categories of Disputes

PBGC stated that it chose two categories of disputes to be eligible for mediation under the new program—''Early Warning Program Matters'' and ''Termination Liability Collection Cases''—because it views them ''as potentially reaping the greatest benefit from mediation.'' A description of these two categories follows.

Early Warning Program Matters

Since the inception of the Early Warning Program in 1993, PBGC has monitored certain employers and identified planned corporate transactions that it believes may result in a significant increase in PBGC's losses in the event of a future plan termination.

PBGC's monitoring efforts focus on controlled groups maintaining plans that, in the aggregate, have: (1) underfunding of $50 million or more; or (2) 5,000 or more participants. *See www.pbgc.gov/prac/risk-mitigation.* However, these criteria do not serve as strict limits on the reach of the Early Warning Program. Informal guidance from PBGC staff notes that, even where a controlled group does not meet either the $50 million screening criterion or the 5,000-participant screening criterion, PBGC may open an Early Warning Program case ''for other reasons as appropriate.'' *See Q&A 20 at www.americanbar.org/content/dam/aba/events/employee_benefits/PBGCQA2016_final.authcheckdam.pdf.*

PBGC has provided the following examples of transactions or events that may be of concern to it under the Early Warning Program: ''change in the group of companies legally responsible for supporting a pension plan (a controlled group)''; ''major divestiture by an employer that retains significantly underfunded pension liabilities''; ''leveraged buyout involving the purchase of a company using a large amount of secured debt''; ''substitution of secured debt for a significant amount of unsecured debt''; and ''payment of a very large dividend to shareholders.'' *See www.pbgc.gov/prac/risk-mitigation.*

If PBGC is concerned about a transaction, it may intervene to seek protection for a pension plan or for itself. PBGC's leverage to extract settlements in Early Warning Program cases is a consequence of its authority under ERISA Section 4042(a)(4) to initiate termination proceedings whenever PBGC determines that ''the possible long-run loss of the [PBGC] with respect to the plan may reasonably be expected to increase unreasonably if the plan is not terminated.''

PBGC has no authority to approve or disapprove a corporate transaction, nor does it have the authority to terminate a pension plan unilaterally. However, if PBGC concludes under its Early Warning Program that a transaction may result in an unreasonable increase in its possible risk of long-run loss, PBGC can threaten to initiate an involuntary termination of a plan unless it is provided with the protection it seeks. PBGC's initiation of an involuntary termination could, in many cases, result in a cascade of potentially catastrophic consequences, including the triggering of various defaults, the increase and acceleration of pension liability, the creation of a new liability for termination premiums, the need to file for bankruptcy protection, and job losses.

Because of the potential consequences of plan termination, even the threat that PBGC might initiate an involuntary termination could significantly destabilize a business. If a transaction is planned, such a threat could scare away lenders and/or other parties to the transaction and thus have the effect of blocking the transaction. However, in threatening—implicitly or explicitly—to initiate an involuntary termination action in an Early Warning Program case, generally PBGC's goal is not to terminate the pension plan, but rather to obtain a settlement that PBGC views as strengthening the plan's financial condition and reducing PBGC's risk.

The most common form of protection PBGC seeks in an Early Warning Program settlement agreement is a commitment to make excess contributions (above and beyond minimum required contributions) to the pension plan, either immediately or over a period of years, with a commitment not to treat the excess contributions as creating or increasing the plan's ''prefunding balance.'' (The prefunding balance is essentially a credit balance that may in certain circumstances be used, dollar-for-dollar, to offset near-term future required contributions.) The excess contribution obligation may be based on a percentage of proceeds from an asset sale or financing.

PBGC may also ask for (or insist on) some form of security through a letter of credit, a surety bond, or a consensual lien (often a junior lien) on assets, as protection in the event of a future failure to meet minimum funding requirements, a failure to satisfy a contractual obligation to make excess contributions, and/or a future distress or involuntary termination resulting in the full plan underfunding (determined on a conservative PBGC plan termination basis) coming due. However, this is relatively rare, as PBGC much prefers the ultimate form of security, *i.e.*, additional cash contributions going into the pension plan. Other settlement options could include (either on a stand-alone basis or in combination with any other options) a negative pledge, a restriction on dividends, or a contractual guarantee by an entity that will no longer bear statutory responsibility for the pension plan as a result of the transaction under review.

These settlement options should not be viewed as an exhaustive listing of ways to settle an Early Warning Program matter with PBGC. Although PBGC is a Federal agency, it has essentially the same flexibility to enter into a settlement agreement on reasonable commercial terms as would any lender or other private party. Thus, there is room for significant creativity in fashion-

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ing an appropriate resolution. The availability of mediation under the pilot program may serve to facilitate the efforts of the parties to find a creative solution so that a transaction of great importance to the employer can be implemented in a timely manner.

Termination Liability Collection Cases

An underfunded single-employer plan covered by Title IV of ERISA may terminate in a voluntary distress termination only if each member of the responsible controlled group meets at least one of four financial distress tests in Title IV of ERISA. Similarly, in considering whether to pursue an involuntary termination of a covered plan, PBGC will take into account the financial status and circumstances of each member of the responsible controlled group. Whether an underfunded plan terminates in a distress termination under ERISA Section 4041(c) or an involuntary termination under ERISA Section 4042, an employer will face significant liabilities.

The key liabilities, all of which PBGC can pursue on a ''joint-and-several'' basis against each member of the controlled group that had been responsible for maintaining the plan, are those for: (1) the plan's ''unfunded plan benefit liabilities'' (determined on a conservative plan termination basis); (2) any unpaid minimum funding contributions; (3) any unpaid annual PBGC premiums and related penalty and interest charges; and (4) a sizeable ''termination premium'' of $1,250 per participant, per year, for three years following plan termination (subject to an exemption for distress terminations based on the liquidation distress test).

Most distress and involuntary terminations involve employers in bankruptcy, where any PBGC mediation efforts are likely to arise under bankruptcy court mediation programs rather than under the new mediation pilot program. And there are many distress and involuntary terminations in which mediation would serve no purpose, as there are no assets available for settlement (and indeed, as noted below, cases where there is a ''limited ability to pay'' are not eligible for mediation under the pilot program). However, there are distress and involuntary terminations that arise outside of bankruptcy where mediation under the pilot program can serve a very useful purpose.

The distress termination test most likely to be met by the members of a controlled group outside of the bankruptcy context is the business continuation test, which requires that the controlled group member demonstrate ''to the satisfaction of [PBGC] that, unless a distress termination occurs, such person will be unable to pay such person's debts when due and will be unable to continue in business.'' A successful distress termination case under the business continuation test—or a successful involuntary termination case (completed consensually) under similar circumstances—generally must also entail a successful resolution of the resulting termination liabilities. This requires that the employer's pension debt be restructured so that it becomes affordable and can be paid without threatening the employer's viability going forward.

As noted above, PBGC has broad authority to settle plan termination-related liabilities with employers. In the case of an ongoing employer that is not in bankruptcy, PBGC will generally attempt to achieve a settlement that allows the employer to continue in business. Of course, PBGC and the employer may have differing views as to what level of immediate or deferred settlement payments would be affordable. The availability of mediation under the pilot program may serve to bridge the gap between PBGC and the employer, and thus be helpful in ensuring that the parties reach an acceptable resolution that enables the employer to survive.

Ground Rules

As discussed above, the pilot program will cover only Early Warning Program Matters and Termination Liability Collection Cases. PBGC's announcement sets forth some basic ground rules that will apply to the program.

Cases Not Eligible for Mediation

In its announcement, PBGC described three circumstances in which cases ''generally'' would not be eligible for mediation under the pilot program. The use of ''generally'' leaves open some flexibility.

The first circumstance in which mediation under the pilot program will generally not be available is where ''[t]he plan sponsor has a minimal ability to pay.'' This circumstance presumably reflects the view that, in most such cases, PBGC will either decide not to pursue the employer (*e.g.*, by writing off the liabilities associated with a plan termination) or reach a settlement with the employer that involves a very low level of payments. On the other hand, there may be cases in which both PBGC and the employer agree that the employer has a ''minimal'' ability (but clearly ''some'' ability) to pay, but nonetheless be unable to reach agreement on how much the employer should pay and when the payments should be made. In such cases, the employer may want to request that PBGC make mediation available as a means to resolve the disagreement.

The second circumstance in which mediation under the pilot program will generally not be available is where ''[t]here is a court proceeding pending.'' Presumably this exclusion does not reflect any unwillingness on the part of PBGC to engage in mediation in connection with court proceedings, but rather reflects only that mediation in such cases will be pursued as appropriate under the auspices of the relevant court. Significantly, PBGC's announcement does not provide for a similar exclusion from the pilot program where there is an ''administrative'' proceeding pending (*e.g.*, an appeal, under PBGC's regulations governing requests for review at 29 C.F.R. Part 4003, to PBGC's Appeals Board of an initial determination of the amount of a plan's ''unfunded benefit liabilities''). Hopefully, the availability of mediation in such circumstances will facilitate a consensual resolution and thereby obviate the need for a court proceeding.

The third and final circumstance in which mediation under the pilot program will generally not be available is where ''[t]here is limited time to act and the plan sponsor has declined to sign a standstill or tolling agreement.'' In an Early Warning Program case, PBGC may need to act before a transaction becomes effective, *e.g.*, to be able to initiate an involuntary termination seeking a termination date that would capture the members of the pre-transaction controlled group. In such a case, PBGC may insist on a standstill agreement so as to allow time for the parties to attempt to resolve PBGC's concerns. Without a standstill agreement in place, there may well be insufficient time for the mediation process to play out. Similarly, in a case where PBGC is nearing the end of the statutory limitations pe-

riod for bringing a court action to collect termination liability (generally six years), mediation may not be feasible if the employer is unwilling to give PBGC more time by signing a tolling agreement.

Mediators

PBGC described the mediation process as ''enabl[ing] parties to resolve disputes with the assistance of a skilled, neutral and independent dispute resolution professional, while maintaining control of the process and its outcome,'' and referenced the ''2016 Report on Significant Developments in Federal Alternative Dispute Resolution'' (available at www.adr.gov/pdf/2016-adr-rpt.pdf) for information on ''how federal agencies can incorporate mediation to save time and cost for both the government and private parties, along with improving stakeholder relations.'' Under the pilot program, mediators ''will be obtained from the Federal Mediation and Conciliation Service (FMCS) through an interagency agreement.''

Mediation Costs

PBGC stated that the parties to a mediation would ''split the costs to prevent any appearance of partiality.'' Presumably this is a reference only to the costs of the mediator, which in many cases will be only a small portion of the overall costs of engaging in mediation (including in particular professional fees). It is worth noting, however, that the bulk of the costs associated with the mediation likely would be incurred even in the absence of mediation, and that, where mediation is successful, the overall costs of reaching a resolution will likely be lower, perhaps significantly so, than if mediation had not been used.

Participants

In its announcement, PBGC stated that its subject matter experts will be trained in mediation practice, and that members of PBGC's case teams will participate in the mediation of their case. Employers are entitled to participate in the mediation ''along with or through the representatives of their choice.'' In the types of cases that are covered by the pilot program, financial issues often loom larger than legal issues. Accordingly, it will generally be helpful for employers to involve their financial officials and any financial advisors, as PBGC will undoubtedly involve their financial officials and any financial advisors.

Timing

PBGC stated that ''[i]n eligible Early Warning engagements, companies shall be advised of the availability of mediation at the outset of negotiation.'' As for the timing of the mediation process itself, PBGC made clear that mediation would be available only ''after PBGC receives sufficient responses to its information requests,'' and that ''the timing of the transaction at issue will determine the window for mediation.'' PBGC also noted that the mediation ''must be completed before the date of the closing, with sufficient time left for the parties to document the mediated resolution or take legal action, if warranted.''

What is not entirely clear is the point at which ''negotiation'' would be treated as having commenced for purposes of determining when PBGC would provide notice of the availability of mediation. In the ordinary course, when PBGC determines that it may have a concern about a transaction under the Early Warning Program, PBGC will contact the employer to gather information, sometimes through one or more phone calls and more often through written requests for information. There will then often be significant back-and-forth discussions or correspondence about the transaction under consideration. The point at which the process moves from information gathering to ''negotiation'' is not marked by a bright line. Nonetheless, if the employer has a need to move quickly in connection with a transaction, whether or not PBGC has officially notified the employer of the availability of mediation under the pilot program, there is nothing that precludes the employer from requesting mediation at an early stage to get the process underway if it appears that mediation may be helpful.

In termination liability collection cases, PBGC stated that it will make mediation available within a reasonable time after it completes its review and analysis of the information that an employer who claims that net worth is limiting is required to submit under 29 C.F.R. § 4062.6. (A determination that net worth is limiting, *i.e.*, that the amount of a plan's ''unfunded plan benefit liabilities'' exceeds 30 percent of the aggregate positive net worth of all members of the controlled group, may at least theoretically lead to more favorable terms for payment of the liability and will lead to a reduction in the amount of any lien based on a neglect or refusal to pay the liability. *See 29 U.S.C. § § 1362(b)(2)(B), 1368(a); 29 C.F.R. § § 4062.9, 4068.4.)* There was no indication in the announcement as to when mediation would be available in the case of an employer who does not claim that net worth is limiting, but employers in such cases should of course consider requesting mediation whenever it appears to be appropriate.

For an employer who claims that net worth is limiting in connection with a distress termination, the deadline for submitting the required supporting information to PBGC under 29 C.F.R. § 4062.6(a)(1)(ii)(A) is the same as the deadline for filing the distress termination notice (Form 601) with PBGC under 29 C.F.R. § 4041.45(a): the 120th day after the proposed termination date. PBGC may of course complete its review and analysis of the net worth information before it reaches a decision on the distress termination application. Thus, an open question is whether PBGC will be willing to engage in mediation regarding a potential settlement that would be contingent on PBGC later approving a distress termination application. (PBGC has engaged in *non-mediated* settlement negotiations in such circumstances.) Even where PBGC has already informed an employer that it has decided to approve a pending distress termination application, the employer may want to negotiate a settlement of the resulting liability before it signs (as the plan administrator of the plan) a termination and trusteeship agreement that would mature that liability, so as to ensure that the matured liability is settled as soon as it arises. In such circumstances, mediation can play a key role in facilitating and expediting the process.

Evaluation of Pilot Program

PBGC stated that, at the end of the one-year pilot program, it will evaluate the program's success according to the following metrics, and include employer feedback as part of the evaluation: ''percent of screened cases found eligible to participate; percent of eligible cases opting for mediation; resolution rate—impact on case inventory; time to resolution; costs savings vs. litigation or protracted negotiations; and outside stake-

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holder reaction to Pilot—impact on stakeholder relationships.''

Conclusion

The availability of mediation under the pilot program is a welcome development, as it clearly signals a heightened awareness on PBGC's part of the importance of enhancing its relationship with its stakeholders and of moving toward methods of resolving disputes that are more cooperative, collegial, and efficient, and correspondingly less adversarial and less costly (in both time and money). In appropriate circumstances, an employer may benefit significantly from the availability of mediation.

Although the pilot program is currently limited to two categories of cases, it has the potential to be expanded to cover virtually any area where there may be a dispute between PBGC and a member of its regulated community. To the extent that practitioners are aware of the program and take advantage of it where appropriate, there should be sufficient experience for PBGC to make informed decisions about the future of the program. PBGC's goals under the program are laudable, and hopefully will be achieved during and after the one-year pilot period.