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PBGC Plays a Stronger Hand in Economy Weakened by Frequent Bankruptcies

The Pension Benefit Guaranty Corporation is aggressively using its statutory options for managing the agency's pension insurance programs and guaranteeing its own solvency ahead of creditors' claims under the federal bankruptcy code, according to employee benefits attorneys and the agency.

An emerging view among employers and practitioners is of a PBGC increasingly inclined to intervene when employers close down operations at any of their facilities. Since 2007, PBGC has employed a previously little-used provision of the Employee Retirement Income Security Act of 1974, ERISA Section 4062(e), to intervene before companies end up in bankruptcy court, where PBGC typically is a general unsecured creditor.

Since March 2007, PBGC has negotiated Section 4062(e) settlements totaling $399.4 million with 18 companies, including Electrolux, Cooper Tire, and Western Union, according to records obtained from PBGC through a Freedom of Information Act request. More than half of those settlements (55 percent) occurred in 2009.

PBGC also has played its hand by:

- using the agency's legal authority to perfect liens on company assets when plan sponsors owe delinquent contributions of $1 million or more;
- enforcing a new rule on variable-rate premiums, collecting termination premiums from failed sponsors, pursuing new claims for post-termination premium payments when former plan sponsors emerge from bankruptcy; and
- taking steps to identify large plans that purchase annuity contracts shortly before standard terminations and developing guidance on purchasing irrevocable commitments before standard terminations.

Increasing Terminations. Jed Brickner, a partner in the New York law office of Latham & Watkins, said PBGC is acting aggressively to protect pensions as its own deficit grows because of increasing business bankruptcies. ''They need to be as active as they possibly can be under these circumstances,'' Brickner told BNA Dec. 2. ''They also have a lot more opportunities to be aggressive,'' he added. In fiscal year 2009, which ended Sept. 30 for PBGC, as many as 144 underfunded single-employer plans were terminated and taken over by PBGC, a nearly 115 percent increase compared with fiscal 2008 (218 PBD, 11/16/09; 36 BPR 2563, 11/17/09).

Economic conditions have provided not only more opportunities but also additional solvency reasons for PBGC to intervene when corporate facilities or operations at any location are shut down, Harold Ashner, former PBGC assistant general counsel for legislation and regulations who is now a partner in the Washington, D.C., law firm of Keightley & Ashner, told BNA Dec. 2. ''It's hard to speculate, but if PBGC were sitting on a huge surplus instead of a huge deficit, it's certainly possible they might view this a little differently. But that's not the world we're operating in,'' Ashner said.

Section 4010 Reporting Notwithstanding its success at negotiating settlements, PBGC also has had its enforcement hand weakened by the Pension Protection Act of 2006 (Pub. L. No. 109-280), which reduced employer reporting obligations that had existed under Section 4010 of ERISA.

Filings under Section 4010 helped PBGC better understand its insurance risks by providing current information on plan assets, liabilities, and underfunding, PBGC spokesman Marc Hopkins told BNA Nov. 18. ''Unfortunately, changes enacted in PPA 2006 have reduced the number of plans that file under [Section] 4010,'' Hopkins said.

Plans that were underfunded by at least $50 million had to file in the past, but now only plans that are below 80 percent funded are subject to Section 4010 reporting requirements. Hopkins added that in 2005, PBGC received Section 4010 information from 450 pension plan sponsors, whereas in 2008, at a time of increased plan underfunding, the agency received that information from only 104 plan sponsors.

However, PBGC has other authority it can use to get information that it wants. The agency announced Nov. 20 that it intends to use its separate authority under ERISA Section 4043 for alternative sources of reporting information. PBGC proposed eliminating most of the automatic reporting waivers and filing extensions that are now permissible under ERISA Section 4043 (223 PBD, 11/23/09; 36 BPR 2674, 11/24/09).

As the agency implements various strategies aimed at achieving future solvency, some lawmakers have proposed rolling back a provision enacted under PPA that permitted PBGC to use a company's bankruptcy filing date for purposes of calculating the amount of pension obligations that the agency would guarantee. PBGC's present and future pension obligations produced a $21.9 billion deficit in fiscal 2009, nearly double its fiscal 2008 deficit of $11.1 billion.

Enforcement Under ERISA Section 4062(e). Under the original authority of ERISA Section 4062(e), PBGC ''is aggressively pursuing liability against downsizing employers,'' Ashner said.

Section 4062(e) empowers PBGC to demand that an employer make escrow payments or post a bond to mitigate the risk of having an underfunded plan terminate in the next five years, Ashner said. The liability is triggered when an employer closes down operations at a facility in any location, creating job losses that put more than 20 percent of the active participants in its pension plan out of work.

In practice, however, PBGC routinely negotiates with employers for alternatives to that statutory liability, Ashner said. Jim Keightley, former PBGC general counsel and now a partner at Keightley & Ashner, told BNA Dec. 2 that the goal in negotiations with PBGC should be to reach a settlement that ''strikes an appropriate balance between PBGC's need for protection and the legitimate business needs of the employer.'' PBGC has said it is developing guidance on that liability (92 PBD, 5/15/09; 36 BPR 1206, 5/19/09).

The pursuit of what Ashner termed ''downsizing liability'' has become a centerpiece of PBGC's enforcement efforts, he said. ''Any amount of pension underfunding when a plan terminates ordinarily is a general unsecured claim by PBGC on the estate of the bankrupt employer, with no priority over the claims of other creditors,'' he said. ''By pursuing this downsizing liability, PBGC can improve its position vis-á-vis other creditors in advance of a bankruptcy,'' he added.

Negotiations With Employers. Before 2007, PBGC did not enforce ERISA Section 4062(e) because it had not yet developed a formula for determining the amount a company owed PBGC when a business decision to cease operations at a facility put the company's pension plan at risk, Nell Hennessy, president of the Washington, D.C., firm Fiduciary Counselors, told BNA Oct. 2.

PBGC has since used its statutory authority under Section 4062(e) to reach settlements that are mutually beneficial, Hennessy said. ''Instead of putting money into an escrow [account], PBGC has been negotiating, and I think appropriately, to put the money into the plan,'' she said. ''That's a win-win for the company: it strengthens the plan, and it strengthens the company's balance sheet,'' she added.

PBGC's active enforcement of Section 4062(e) might also be causing some companies to reconsider their plans to shut down certain facilities, Hennessy said. Officials who otherwise might have shut down a facility could decide that keeping it open at some level rather than paying additional fees to PBGC makes sense financially and economically, she added.

Western Union, which reached a $4.1 million negotiated settlement with PBGC in August after shutting down the company's call center in Bridgeton, Mo., declined Dec. 1 to talk with BNA about the negotiation process that resulted in Western Union Financial Services making a $4.1 million cash payment to its pension plan for the 2008 calendar year (161 PBD, 8/24/09; 36 BPR 1946, 8/25/09).

The Section 4062(e) settlements that PBGC has negotiated since March 2007 have affected a total of 49,346 plan participants, including 4,665 at companies such as Revlon, Fresh Del Monte, and Hanesbrands, according to PBGC documents. ''Each 4062(e) agreement is unique,'' PBGC's Hopkins told BNA Nov. 19. ''In some cases, cash is placed immediately into the pension plan,'' he said. In others, a letter of credit is issued or a credit balance is erased. ''The payments are in addition to any required contributions to the plan,'' he added.

Lien Enforcement. In addition to negotiating ERISA settlements, PBGC also has intervened ahead of bankruptcy in cases in which an employer's total unpaid contributions to its pension plan exceed $1 million. Under those circumstances, PBGC can file and enforce tax liens on all members of an employer's controlled group under Section 430(k) of the tax code. Since Oct. 1, 2008, PBGC has filed liens totaling $344 million on the assets of sponsors of 22 pension plans, PBGC's Hopkins told BNA Nov. 18.

Bankruptcy law, which requires PBGC to take all the steps necessary to file a lien before bankruptcy proceedings begin, prevents the agency from completing the lien once the bankruptcy process is under way. ''That's an extremely powerful tool to be considered very seriously,'' said Bill Beyer, former PBGC deputy general counsel and now of counsel to Keightley & Ashner, referring to the financial consequences of PBGC's tax lien authority. Some companies, aware of that lien authority, file for bankruptcy the day before employer contributions to the pension plan are due because a stay begins on the day an employer files a bankruptcy petition, Beyer told BNA Dec. 2. The stay blocks any liens from being filed against the employer, he said.

Changes in Premiums. **Variable-Rate Premiums:** Recent increases in PBGC insurance premiums have helped the agency raise revenue to meet its obligations to pension participants. For plan years starting in 2008, a new rule enacted by PPA required PBGC to eliminate an exemption that allowed companies with fully funded pension plans to avoid paying annual variable-rate premiums. Those premiums cost single-employer plan sponsors $9 for each $1,000 of pension underfunding.

PPA eliminated the full-funding exemption and changed the interest rate rules for determining a plan's present value of vested benefits for variable-rate premium purposes, according to PBGC spokesman Jeffrey Speicher. To determine the present value of vested benefits, employers can use a rate based on the corporate bond yield curve or the discount rate they use for pension funding purposes, Speicher told BNA Nov. 25.

PBGC's variable-rate premium income from single-employer plans increased by $458 million to $699 million during the 2009 fiscal year, a more than 50 percent increase that reflected PBGC's estimates of greater plan underfunding in 2009 and the PPA provision that eliminated the variable-rate premium exemption for single-employer plans, according to PBGC's fiscal 2009 Annual Management Report. In fiscal 2008, PBGC collected $241 million in variable-rate premiums from single-employer plans.

Termination Premiums: Another potential source of premium income for insuring pensions are termination premiums, according to PBGC's latest financial statements. When PBGC terminates a single-employer pension or an employer makes a distress termination but does not liquidate its business, the employer must pay a termination premium, which is generally $1,250 per participant payable for a three-year period. The PPA gave PBGC authority to begin charging termination premiums in 2007. In fiscal 2009, Speicher said, PBGC recognized on its books more than $590 million in termination premium revenue, a more than 10 times increase compared with $57 million in fiscal 2008. The $590 million in termination premium revenue was recognized in fiscal 2009 but not collected, Speicher said.

Termination premiums are becoming a significant factor in bankruptcy reorganization, Brickner said, adding that the U.S. Court of Appeals for the Second Circuit ruled earlier this year that termination premium liability is not dischargeable in a Chapter 11 bankruptcy. ''It's a very big thing, because it means when you are planning how your bankruptcy is going to work, and what assets are still going to be there, you've got to take account of this premium, which can be a very significant amount,'' he said.

Depending on the size of the plan, termination premiums could make a difference in whether a company reorganizes or liquidates, Ashner told BNA. The Second Circuit decision in *Pension Benefit Guaranty Corporation v. Oneida Ltd.* (67 PBD, 4/10/09; 36 BPR 910, 4/14/09) 46 EBC 1911 (2d. Cir. 2009) and (84 PBD, 5/5/09; 36 BPR 1163, 5/12/09) is not binding in other circuits, Ashner said. But if the Second Circuit decision becomes the prevailing law, companies could find in some cases that reorganization is not feasible, he said. Ashner added that he expected PBGC lawyers would continue to make the argument that the liability for termination premiums is not dischargeable in bankruptcy reorganizations.

Irrevocable Commitments. Beyond implementing tougher premium provisions to secure adequate funding for its obligations, PBGC is taking steps to provide guidance to companies that buy annuities immediately before they terminate their pension plans. On Nov. 20, the agency issued a request for public comments on this practice as it gathers information on whether purchases of irrevocable commitments violate statutory and regulatory termination requirements (223 PBD, 11/23/09; 36 BPR 2675, 11/24/09).

PBGC said in the request for comments that it is concerned that those irrevocable annuity purchases could circumvent the procedural protections in the standard termination process. The agency also said that plans might have insufficient assets to pay pension benefits when a plan is terminated and its assets are distributed if plan assets are used to buy irrevocable annuities before the plan is terminated.

Employers, on the other hand, want to know what a standard termination process will cost before they go through the process, Ashner said. ''They don't like surprises, and annuity prices can move significantly,'' he said. ''They might want to be able to find some mechanism for locking in the cost of a standard termination either at or before the beginning of the process rather than wait until the end and find out the cost has gone up and that a standard termination may no longer be affordable.''

Revising Current Law. Further law changes could affect PBGC's ability to finesse its pension obligations. Rep. Earl Pomeroy (D-N.D.), a member of the House Ways and Means Committee, released draft legislation Aug. 27 that would change the date used to calculate the amount of pension obligations guaranteed by PBGC (206 PBD, 10/28/09; 36 BPR 2462, 11/3/09).

Pomeroy's proposal would undo a provision in PPA that PBGC had wanted, which was to begin with the date that a plan sponsor declares bankruptcy for purposes of calculating its pension guarantee, a member of Pomeroy's staff told BNA Dec. 3. The proposal to have PBGC calculate its benefit guarantee based on benefits accrued at the time a pension is terminated rather than when the employer files for bankruptcy, which is usually the earlier of the two, was a change sought by the AFL-CIO, the staff member said. ''Union representatives have always felt that what was done in PPA. . .was a major change that they never agreed with,'' the staff member said. ''It's really more of a protection for workers. Their members would perhaps get a few more months of accrual.''

PBGC has been aggressive in using its statutory authority to manage its pension obligations, but whether rolling back the PPA provision would lessen or increase the agency's insurance risk is anything but certain, a tax law scholar told BNA. ''PBGC in recent years has become much more proactive, whereas in the old days they'd simply wait for the sky to fall and then decide what to do,'' David Pratt, professor of tax and employee benefits law at Albany Law School, Albany, N.Y., said Dec. 4. However, whether it would be good policy to make a plan's termination date the basis for calculating PBGC's pension obligations is uncertain, Pratt said. The outcome would depend on the financial markets and the facts of each case, he added. Even a relatively short period between bankruptcy and termination ''could make a significant difference in the value of the assets and the potential shortfall'' that PBGC would be obligated to cover to guarantee that employees receive their pensions, he said.

By Florence Olsen