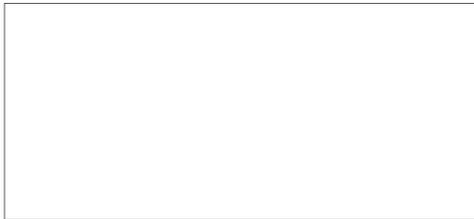




Pension Benefit Guaranty Corporation  
1200 K Street, N.W., Washington, D.C. 20005-4026

September 27, 2013



Re: Consolidated Appeal; Case No. 205441; Delta Pilots Retirement Plan

Dear Messrs. :

The Appeals Board of the Pension Benefit Guaranty Corporation (“PBGC”) reviewed your appeal on behalf of certain participants and beneficiaries (“the appellants”) of the Delta Pilots Retirement Plan (the “Pilots Plan” or the “Plan”). As stated on pages 3 and 4, your appeal lists 13 issues that relate to the benefits the appellants are entitled to receive from PBGC.

As explained in this decision:

- You requested that PBGC conduct another audit of the Pilots Plan’s assets. The Appeals Board confirmed with senior PBGC officials that PBGC has hired a public accounting firm to perform a Plan asset re-evaluation. PBGC will keep Plan participants, beneficiaries, and alternate payees updated on the status of the Plan asset re-evaluation on the [www.pbgc.gov](http://www.pbgc.gov) public website;
- Although we found that Delta and PBGC generally calculated Plan benefits correctly, the Appeals Board found errors in the Social Security reduction for six appellants. The Board corrected the PBGC-payable benefit for these six appellants, as explained in the discussion of Issue #7;
- You reserved the right for individual appellants to supplement your appeal filing and to raise additional individual issues. The Board permitted your firm to supplement your October 28, 2011 appeal filing, and the Board permitted the appellants to raise individual appeal issues;
- The Appeals Board denied your request for the Board to hold a hearing; and
- The Appeals Board denied your appeal with respect to all other issues you raised.

## INTRODUCTION

PBGC is the United States government agency that provides pension insurance in accordance with the Employee Retirement Income Security Act of 1974, *as amended* ("ERISA").<sup>1</sup> If a plan sponsor is unable to support its pension plan, PBGC becomes trustee of the plan and pays pension benefits provided by the plan, subject to legal limitations set by Congress under ERISA.

On September 2, 2006, the Pilots Plan terminated without sufficient assets to pay all of its benefits. PBGC became trustee of the Pilots Plan on December 31, 2006. PBGC sent initial (formal) Benefit Determination letters to the vast majority of the appellants in 2010 and 2011.<sup>2</sup>

On October 28, 2011, you filed a 50-page appeal brief with exhibits ("Appeal Brief" or "AB") on behalf of 1,784 participants and beneficiaries of the Plan.<sup>3</sup> On April 30, 2012, you supplemented your Appeal Brief by submitting to the Appeals Board a 4-page letter (the "Supplemental Appeal Brief" or the "AB Supp.") that presented additional assertions regarding three issues of the AB. In addition, on April 30, 2012 you identified certain errata in the October 28, 2011 Appeal Brief and you provided the Board with a corrected Appeal Brief as well as a number of supplemental exhibits.

The Appeals Board sent you a letter dated August 7, 2012 that: (1) provided you with documents the Board obtained from the Air Lines Pilots Association, International ("ALPA"); (2) stated that the Board preliminarily decided not to grant your request for a hearing; and (3) offered you the opportunity to supplement your hearing request. On September 21, 2012, you responded to the Board's August 7, 2012 letter by submitting a 9-page letter ("Sept. 2012 Letter") with 5 enclosures. You also supplemented the Appeal Brief on May 3, 2013 ("May 2013 Letter"), which included two exhibits that you obtained from PBGC pursuant to a Freedom of Information Act ("FOIA") request.

We refer to the corrected Appeal Brief, the Supplemental Appeal Brief, the Sept. 2012 Letter, the May 2013 Letter, and all exhibits you provided to the Appeals Board collectively as

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<sup>1</sup> 29 United States Code ("U.S.C.") §§ 1301-1461 (2006 & Supp. IV 2010). This decision generally cites the applicable sections of ERISA without providing the parallel U.S.C. citations.

<sup>2</sup> Part 4003 of PBGC's regulations establishes the rules governing PBGC's issuance of initial Benefit Determinations and the procedures for requesting and obtaining administrative review. *See* 29 Code of Federal Regulations ("C.F.R.") § 4003 (titled "Rules for Administrative Review of Agency Decisions"). An initial (formal) Benefit Determination is the letter PBGC issues to communicate the Agency's determination of an individual's benefit. *See* 29 C.F.R. § 4003.21. If the individual desires Appeals Board review of his or her benefit, the individual or his or her representative must file an appeal of the Agency's determination, or request an extension of time to file an appeal, within 45 days from the date of issuance of the Benefit Determination. *See* 29 C.F.R. §§ 4003.4, 4003.52.

<sup>3</sup> You initially appealed on behalf of 1,784 participants and beneficiaries. As addressed in this decision, the Appeals Board determined that 1,498 of the participants and beneficiaries you represent had timely-filed appeals. *See* Enclosure 1 for a list of timely-filed appellants.

the "Appeal." The Appeal consisted of more than 2,000 total pages. Unless otherwise indicated, all citations to the Appeal in this decision refer to the corrected Appeal Brief you provided on April 30, 2012.

The Appeals Board concluded that the Appeal was timely filed for 1,498 of your clients. The Appeals Board did not docket appeals for approximately 300 of your clients because their appeal filings were not timely. You argue that these individuals should be considered appellants with timely-filed appeals.

The Appeals Board concluded that the appeals of the 1,498 Pilots Plan participants and beneficiaries you represent arise out of the same or similar facts and seek the same or similar relief. The Board exercised its discretion under PBGC regulation 29 C.F.R. § 4003.56 to consolidate the appeals of these 1,498 individuals.

#### **LIST OF ISSUES RAISED IN THE APPEAL**

Appellants are a unique class of individuals because they all were in pay status (retired) or eligible to enter pay status (eligible to retire) three years before the Pilots Plan terminated. Thus, all of the appellants are eligible for benefits in Priority Category 3 ("PC3") under the asset allocation provisions in ERISA § 4044. PC3 benefits are discussed in detail in this decision.

The Appeal raises 13 issues, which we have grouped into 5 categories. The Appeals Board responded to the issues in the same order that you presented them in the Appeal. The 13 issues are as follows:

#### **A. PBGC's determination of PC3 benefit amounts:**

**Issue 1:** Whether PBGC correctly concluded that PC3 benefits do not include benefit increases resulting from: (1) the increased Internal Revenue Code ("IRC") § 401(a)(17) compensation limit that was enacted into law in June 2001; and (2) cost-of-living adjustments ("COLAs") to the IRC § 401(a)(17) limit for the years 2004 and 2005. AB at 6-13.

**Issue 2:** Whether PBGC correctly concluded that PC3 benefits do not include benefit increases for "retired pilots" resulting from: (1) the increased IRC § 415(b) limit on benefit payments that was enacted into law in June 2001; and (2) the IRC § 415(b) COLAs for the years 2004, 2005, and 2006. AB at 14-17.

**Issue 3:** Whether PBGC correctly concluded that ERISA does not provide for actuarial increases to PC3 benefits for pilots who were eligible to retire three years before Plan termination, but had later benefit start dates because they remained employed by Delta. AB at 18-24.

**B. PBGC's allocation of assets and recoveries:**

**Issue 4:** In allocating the Plan's assets and PBGC's recoveries to benefit liabilities, whether PBGC disregarded \$1 billion or more in funds that allegedly "left the Plan just before PBGC assumed its role as statutory trustee." AB at 24-26 and 29-30.

**Issue 5:** Whether PBGC: (A) correctly valued the funds it recovered from Delta after the Plan's termination; and (B) correctly applied IRC limits when it allocated the ERISA § 4022(c) amount to benefits in Priority Category 5 ("PC5"). AB at 27-31.

**C. PBGC's payment of guaranteed benefits:**

**Issue 6:** Whether PBGC correctly interpreted and applied the ERISA provisions applicable to guaranteed benefit amounts. AB at 31-36.

**D. PBGC's benefit calculations:**

**Issue 7:** Whether PBGC properly calculated benefits for participants who were eligible to have their benefits calculated under the Plan's Minimum Benefit formula. AB at 36-38.

**Issue 8:** Whether PBGC applied the Social Security Administration Offset at an earlier age than the Plan's provisions authorized. AB at 38-39.

**E. Other claims:**

**Issue 9:** Whether PBGC should re-audit the Pilots Plan's assets. AB at 40-41 and AB Supp. at 2-3.

**Issue 10:** Whether PBGC's application of its appeal time limits improperly denied some individuals the right to join the Appeal. AB at 41-45 and AB Supp. at 3.

**Issue 11:** Whether individual appellants may supplement the Appeal and raise additional individual issues. AB at 45-46.

**Issue 12:** Whether PBGC failed to meet its fiduciary responsibility to the appellants. AB at 45-48 and AB Supp. at 3.

**Issue 13:** Whether the Appeals Board should grant the Appeal's request for a hearing. AB at 49-50.

## OVERVIEW OF THE APPEAL AND THE BOARD'S DECISION

When the Pilots Plan terminated, its total underfunding – i.e., the difference between the values of its assets and its benefit liabilities – exceeded \$2.5 billion.<sup>4</sup>

PBGC's guarantee under ERISA ensures that pension plan participants and beneficiaries will receive their pension benefits up to the statutory limits even if their terminated plan has no assets. Because the Pilots Plan had some assets when it terminated and because PBGC obtained significant recoveries from Delta, ERISA authorizes PBGC to pay additional nonguaranteed benefits to Pilots Plan participants and beneficiaries.

Overall, PBGC is paying over \$1.8 billion of the Pilots Plan's nonguaranteed benefits, in addition to over \$1.6 billion in guaranteed benefits.<sup>5</sup> Nevertheless, PBGC is unable to pay nearly \$1.1 billion of the Plan's benefits.<sup>6</sup>

PBGC is unable to pay all Pilots Plan benefits primarily because ERISA places a cap, known as the Maximum Guaranteed Benefit ("MGB") limit, upon the amounts that PBGC guarantees. For the Pilots Plan, the MGB is \$47,659 per year for a participant who begins receiving PBGC benefits at age 65 in the form of a straight life annuity ("SLA"). Because the large majority of appellants have Plan benefits that exceed the MGB, PBGC is often unable to guarantee their full Plan benefit amounts.

The first four issues and Issue #5.B. of the Appeal assert that PBGC incorrectly determined appellants' PBGC-payable benefits in the PC3 and PC5 priority categories under ERISA. These issues do not affect appellants' guaranteed benefit amounts, which are limited by the MGB. The first four issues and Issue #5.B. relate to how PBGC distributes nonguaranteed benefits to participants and beneficiaries based on the allocation of the Pilots Plan's assets and PBGC's recoveries.

The values of the Pilots Plan's assets and PBGC's recoveries, however, are fixed. If the Appeals Board changes how PBGC-payable benefits in PC3 and/or PC5 are determined, the

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<sup>4</sup> PBGC determined that the Pilots Plan had \$1,984,977,782 in assets and \$4,552,657,782 in benefit liabilities as of its September 2, 2006 termination date, which results in an unfunded benefit liability of \$2,567,680,000 [i.e., \$4,552,657,782 (Plan benefit liabilities) - \$1,984,977,782 (Plan assets) = \$2,567,680,000 (total Plan underfunding)]. See PBGC's *Actuarial Case Memo for Delta Pilots Retirement Plan* ("Actuarial Case Memo") at 1, 30. Appeal Exhibit 5 is a copy of the Actuarial Case Memo, without its appendices and enclosures.

<sup>5</sup> PBGC determined that the "Present Value of Termination Benefits," i.e., the present value of the benefits PBGC pays, is \$3,464,870,978 as of the Pilots Plan's termination date. See Actuarial Case Memo at 1. PBGC valuation data not included in the Actuarial Case Memo show that \$1,815,296,490 of this \$3,464,870,978 present value is for nonguaranteed benefit amounts.

<sup>6</sup> Specifically, the benefits liabilities that PBGC is unable to pay is the difference between the Pilots Plan's total benefit liability (\$4,552,657,782) and the Present Value of Termination Benefits (\$3,464,870,978), which is \$1,087,786,804. See Actuarial Case Memo at 1.

result would be that some Pilots Plan participants and beneficiaries would be entitled to larger PBGC-payable benefit amounts and others would be entitled to smaller benefit amounts. Accordingly, the relief sought in the first four issues of the Appeal and Issue #5.B., if granted in full or in part, essentially would create “winners” and “losers” as compared to how PBGC currently allocates Pilots Plan’s assets and PBGC’s recoveries to benefits.

The Appeals Board decided that PBGC correctly determined benefits in the PC3 and PC5 priority categories and correctly allocated Pilots Plan assets and PBGC’s recoveries to benefits in accordance with ERISA and PBGC regulations. Thus, we denied the first four issues of the Appeal and Issue #5.B. The Appeal Board resolved the remaining issues of the Appeal as follows:

- Issue #5.A. contends that PBGC incorrectly calculated PBGC’s recovery on its claims against Delta. The Board found no error in PBGC’s recovery calculation.
- Issue #6 challenges PBGC’s longstanding interpretation of its guarantee obligation. The Appeals Board applied its prior precedent, which was affirmed by a recent federal District Court decision, in rejecting the Appeal’s position on this issue.
- Issues #7 and #8 address how PBGC calculated Plan benefit amounts for certain appellants. The Board found and corrected errors in the Social Security offsets for six appellants. With the exception of these errors, the Board found that PBGC correctly computed appellants’ benefits.
- Issue #9 requests a new audit of the Pilots Plan’s assets. As stated at the beginning of this decision, PBGC has hired a public accounting firm to perform a Plan asset re-evaluation.
- Issues #10 through #13 concern procedural matters. As requested in Issue #11, the Appeals Board permitted the appellants to raise individual appeal issues that affect their benefits. The Board denied the other procedural requests in the Appeal.

The Board’s decision on the Appeal is the final Agency action for all the appellants except those with pending individual appeals.<sup>7</sup>

## **BACKGROUND**

### ***The Plan’s Termination and Trusteeship.***

Delta Air Lines, Inc. (“Delta”) established the Pilots Plan effective February 1, 1972. On September 14, 2005, Delta and 18 Delta subsidiaries filed petitions for relief under Chapter 11 of the United States Bankruptcy Code in the United States Bankruptcy Court for the Southern District of New York (the “Bankruptcy Court”).

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<sup>7</sup> The Board will issue a separate decision to each appellant with a pending individual appeal.

On June 19, 2006, Delta issued Notices of Intent to Terminate the Plan (“NOITs”) pursuant to ERISA § 4041(a)(2); the NOITs proposed September 2, 2006 as the Date of Plan Termination (“DOPT”). Delta timely filed a NOIT with PBGC. On August 4, 2006, Delta filed a motion in the Bankruptcy Court seeking a ruling that Delta and its 18 subsidiaries met the criteria under ERISA § 4041(c)(2)(B)(ii)(IV) for the voluntary distress termination of the Pilots Plan.

On September 5, 2006, the Bankruptcy Court approved Delta’s distress termination motion.<sup>8</sup> PBGC notified Delta on December 15, 2006 that PBGC had determined: (1) Delta and each member of its controlled group met ERISA’s criteria for a distress termination;<sup>9</sup> and (2) PBGC was unable to find that the Pilots Plan’s assets were sufficient for guaranteed benefit liabilities as of the proposed termination date.<sup>10</sup>

PBGC and Delta executed a Settlement Agreement on December 4, 2006 that, among other things, resolved the claims that PBGC filed on its own behalf and on behalf of the Pilots Plan in Delta’s bankruptcy proceeding. The Bankruptcy Court approved this Settlement Agreement on December 20, 2006.

Effective December 31, 2006, PBGC and the Pilots Plan’s administrator executed an agreement providing for: (1) the termination of the Pilots Plan; (2) establishment of September 2, 2006 as the Pilots Plan’s DOPT; and (3) appointment of PBGC as the statutory trustee of the Pilots Plan under ERISA § 4042. As a result of this agreement, PBGC became the Pilots Plan’s trustee on December 31, 2006.

Delta exited bankruptcy on April 30, 2007 and remains an active carrier in the airline industry.

### **PBGC’s Guarantee and Its Limits.**

The pension benefit a retiree receives from PBGC initially depends on the plan’s provisions; PBGC does not pay more than the plan would have paid (except in limited situations where the plan failed to follow ERISA’s requirements). Moreover, PBGC does not guarantee all benefits provided by a pension plan. To be guaranteed, a benefit must, first, be “nonforfeitable,” which means that the participant must have satisfied the pension plan’s requirements to be eligible for

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<sup>8</sup> The Bankruptcy Court found that Delta and the 18 subsidiaries in bankruptcy each met the distress termination requirement under ERISA § 4041(c)(2)(B)(ii)(IV). Specifically, the Bankruptcy Court found that, unless the Pilots Plan terminates, each Debtor would be unable to obtain exit financing that would enable it to emerge from bankruptcy, submit a feasible plan of reorganization under 11 U.S.C § 1129, pay all debts pursuant to a plan of reorganization, and continue in business outside of Chapter 11.

<sup>9</sup> Specifically, PBGC determined that Delta and its controlled group met the distress termination criteria set forth in ERISA § 4041(c)(2)(B) and 29 C.F.R. §§ 4041.41(c), 4041.46.

<sup>10</sup> See ERISA § 4041(c)(3)(A) (determinations by PBGC relating to plan sufficiency for guaranteed benefits and for benefit liabilities).

the benefit by the date on which the plan terminates.<sup>11</sup> Not all nonforfeitable benefits are guaranteed; there are statutory and regulatory limits on PBGC's guarantee.

As previously stated, the MGB is a statutory cap on the amount of PBGC's guarantee.<sup>12</sup> The amount of an individual's MGB depends on a number of factors, including the year in which the pension plan terminated, the participant's age at the later of DOPT or date of benefit commencement, the form in which the benefit is paid, and the age of the participant's spouse if the benefit form includes a surviving spouse benefit.<sup>13</sup> For plans terminating in 2006, as the Plan did, the MGB is \$3,971.59 per month (\$47,659 per year) for a participant who begins receiving PBGC benefits at age 65 in the form of a straight life annuity ("SLA") with no survivor benefit. If the person is younger than 65 and if a survivor benefit will be paid (for example, to a spouse), the MGB is lower.<sup>14</sup>

Another limit on PBGC's guarantee is the phase-in limit, which provides that PBGC's guarantee of a benefit increase is phased in over five years from the later of the adoption or effective date of the increase.<sup>15</sup> To determine the phase-in limit, PBGC must scrutinize all plan amendments made during the five years before a plan terminates. Because PBGC applies the MGB limit before applying the phase-in limit, the number of participants whose guaranteed benefit is decreased by the phase-in limit is substantially less than the number of participants affected by the MGB. The Appeal does not raise any issues regarding PBGC's application of the phase-in limit.

In many cases, whether a participant receives his or her full plan benefit depends principally on the statutory and regulatory limits on PBGC's guarantee. But, if a plan has enough assets, some participants may receive more than the guaranteed amount.

#### **Allocating a Pension Plan's Assets and PBGC's Recoveries Under ERISA.**

ERISA's six-tier asset allocation structure determines how a terminated pension plan's assets are distributed among various categories of benefits when the assets are insufficient to pay all promised benefits. The six priority categories are referred to as "PC1," "PC2," "PC3," etc. The Pilots Plan has no benefits in the first two priority categories (PC1 and PC2), which relate to benefits derived from a participant's own contributions. The next priority category, PC3, covers a participant's or beneficiary's benefits that were "in pay status" (i.e., were being paid) three or more years before the plan's termination date, or that would have been in pay status three years

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<sup>11</sup> See ERISA § 4001(a)(8); 29 C.F.R. § 4022.3(a)(1).

<sup>12</sup> See ERISA § 4022(b)(3).

<sup>13</sup> See 29 C.F.R. § 4022.23.

<sup>14</sup> See 29 C.F.R. §§ 4022.22, 4022.23.

<sup>15</sup> See ERISA § 4022(b)(1), (7); 29 C.F.R. §§ 4022.2, 4022.24, 4022.25.

before termination if the participant had retired. PC4 generally covers benefits guaranteed by PBGC. PC5 covers other nonforfeitable benefits (generally, benefits that are not in PC3 and are not guaranteed due to the limits described above). PC6 covers all other benefits under the plan (i.e., non-vested benefits).

Because PC3 benefits come ahead of PBGC-guaranteed benefits (PC4) in the allocation structure, a participant or beneficiary who went into pay status (or could have gone into pay status) three or more years before plan termination potentially may receive his or her full plan benefit amount, even if it is not all guaranteed by PBGC. This would occur if all of a participant's benefit is in PC3 and the plan's assets are sufficient to cover all benefits in PC3.

If a plan's assets do not cover all benefits in PC3, each participant or beneficiary with a PC3 benefit generally will receive a pro rata share of the assets.<sup>16</sup> PBGC determined that the Pilots Plan's assets as of DOPT (\$1,984,977,782) covered 93.03847% of the Pilots Plan's benefits in PC3.<sup>17</sup>

As provided under ERISA § 4022(c), PBGC pays some participants and beneficiaries additional benefits based on PBGC's recoveries for Unfunded Benefit Liabilities ("UBL"). Essentially, the UBL is the shortfall between a plan's assets and its liabilities for benefits.<sup>18</sup> For pension plans like the Pilots Plan, in which the outstanding amount of Unfunded Non-Guaranteed Benefits ("UNGB") exceeds \$20 million, the ERISA § 4022(c) amounts payable to participants and beneficiaries are determined based on PBGC's actual recovery on its claims against the plan sponsor. Thus, as provided under ERISA § 4022(c), PBGC allocated a portion of its UBL recoveries from Delta to Plan benefits that are neither guaranteed by PBGC, nor funded by the Plan's assets.

For the Pilots Plan, the ERISA § 4022(c) amount funds all UNGB in PC3. Thus, through the allocation of the Pilots Plan's assets, PBGC's guarantee of benefits up to the statutory limits, and PBGC's recoveries, Plan participants and beneficiaries entitled to PC3 benefits are receiving 100% of their benefit amounts in PC3. Additionally, as explained more fully in our discussion of Issue #5, the ERISA § 4022(c) amount funds a portion of the benefits in PC5.

**Delta's Related Pension Plans: the Supplemental Annuity Plan, the Bridge Plan, and the Money Purchase Pension Plan.**

Under the Delta pension program in effect before the Pilots Plan terminated, benefits paid from the Pilots Plan were coordinated with the benefits payable from two nonqualified defined benefit plans and one tax-qualified defined contribution plan, each of which terminated on or

<sup>16</sup> See ERISA § 4044(b)(2); 29 C.F.R. § 4044.10(d).

<sup>17</sup> See Actuarial Case Memo at 30.

<sup>18</sup> See ERISA § 4001(a)(18) (definition of UBL) and § 4062(b) (liability of a plan sponsor and its controlled group to PBGC for UBL).

before the Pilots Plan's DOPT of September 2, 2006.<sup>19</sup> The two nonqualified plans are: (1) the Delta Pilots Supplemental Annuity Plan ("SAP");<sup>20</sup> and the Delta Pilots Bridge Plan ("Bridge Plan").<sup>21</sup> The tax-qualified defined contribution plan is the Delta Money Purchase Pension Plan ("MPPP").

As a result of Delta's bankruptcy, Delta did not pay benefits under the SAP and under the Bridge Plan after September 1, 2005. Benefits payable under the MPPP were distributed to its participants and beneficiaries upon the MPPP's termination. Because the SAP, Bridge Plan, and MPPP were not tax-qualified defined benefit plans covered by Title IV of ERISA, PBGC is not responsible for the benefits provided under those plans.<sup>22</sup> The Appeal does not raise any issues involving the SAP, Bridge Plan, and MPPP.

### **The Pilots Plan's Formal Documents.**

The last formal plan document that restated all of the Pilots Plan's terms is the *Delta Pilots Retirement Plan Amended and Restated Effective As of July 1, 1996* (the "1996 Restatement"). Delta, as Plan sponsor, adopted the 1996 Restatement on April 14, 1998. Delta later adopted thirteen Pilots Plan amendments. In Enclosure 2, we provide a copy of the 1996 Restatement and its thirteen amendments.

### **The Appeals Board's Prior Decision in the US Airways Group Appeal.**

Several issues and legal arguments presented in the Appeal were previously presented to the Appeals Board in an appeal filed on behalf of a group of US Airways pilots (the "US Airways Pilots Plan Appeal").<sup>23</sup> For example, Issue #3 and Issue #6 of the Appeal essentially raise the same issues that previously were raised in the US Airways Pilots Plan Appeal.

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<sup>19</sup> The Pilots Plan's benefit coordination provisions are complex. Certain aspects of these provisions are explained in more detail in Issues #7 and #8.

<sup>20</sup> The SAP provided benefits that could not be paid from the Pilots Plan due to compensation limits under IRC § 401(a)(17).

<sup>21</sup> The Bridge Plan provided benefits that could not be paid from the Pilots Plan due to benefit payment limits under IRC § 415(b).

<sup>22</sup> ERISA § 4021 addresses PBGC's coverage of pension plans.

<sup>23</sup> The US Airways Pilots Plan Appeal was filed in March 2007 on behalf of nearly 800 US Airways pilots who were participants in the terminated Retirement Income Plan for Pilots of US Airways, Inc. ("US Airways Pilots Plan"). The Appeals Board consolidated the appeals of the appellants named in the US Airways Pilots Plan Appeal.

In a February 29, 2008 Appeals Board decision (“US Airways Decision”), the Board analyzed and decided most of the issues raised in the US Airways Pilots Plan Appeal.<sup>24</sup> The Board also issued a decision on June 5, 2009 (“2009 Decision”) that responded to additional claims.<sup>25</sup> Copies of those decisions (without their Appendices and Enclosures) are provided as Enclosures 3 and 4, respectively, to this decision.<sup>26</sup>

After Appeals Board decisions in the US Airways Pilots Plan Appeal were issued, the appellants in that case challenged almost all of the Board’s rulings in a legal action (the “*Davis*” case) filed in the United States District Court for the District of Columbia (“District Court”). On May 30, 2012, the District Court issued a decision in *Davis* that upheld the Appeals Board’s rulings in the US Airways Decision and the 2009 Decision.<sup>27</sup>

The plaintiffs in *Davis* subsequently challenged the District Court’s rulings in an appeal filed with the United States Court of Appeals for the District of Columbia (“Circuit Court”). The Circuit Court heard oral arguments, but it has not yet issued a ruling.

#### **A. PBGC’S DETERMINATION OF PC3 BENEFIT AMOUNTS**

The first three issues of the Appeal address how PBGC determined benefit amounts in Priority Category 3 (“PC3”).

As stated in the Introduction, ERISA § 4044(a) establishes a hierarchy for allocating plan assets to benefit liabilities upon a plan’s termination. PC3 is defined in ERISA § 4044(a)(3) as follows:

- (a) Order of Priority of Participants and Beneficiaries. – In the case of the termination of a single-employer plan, the plan administrator shall allocate the assets of the plan (available to provide benefits) among the participants and beneficiaries of the plan in the following order:

...

- (3) Third, in the case of benefits payable as an annuity-

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<sup>24</sup> On dates after February 29, 2008, the Appeals Board issued additional decisions related to the US Airways Pilots Plan.

<sup>25</sup> The 2009 Decision addresses the benefits of a US Airways pilot who received a PBGC benefit determination after the US Airways Decision was issued. The appeal filed on behalf of this pilot incorporated by reference the issues presented in the US Airways Pilots Plan Appeal, in addition to raising new issues.

<sup>26</sup> Personal information was redacted (i.e. removed) from Enclosures 3 and 4.

<sup>27</sup> *Davis v. PBGC*, 864 F.Supp.2d 148 (D.D.C. 2012), *appeal docketed*, No. 12-5274 (D.C. Cir., Dec. 28, 2012).

(A) in the case of the benefit of a participant or beneficiary which was in pay status as of the beginning of the 3-year period ending on the termination date of the plan, to each such benefit, based on the provisions of the plan (as in effect during the 5-year period ending on such date) under which such benefit would be the least,

(B) in the case of a participant's or beneficiary's benefit (other than a benefit described in subparagraph (A)) which would have been in pay status as of the beginning of such 3-year period if the participant had retired prior to the beginning of the 3-year period and if his benefits had commenced (in the normal form of annuity under the plan) as of the beginning of such period, to each such benefit based on the provisions of the plan (as in effect during the 5-year period ending on such date) under which such benefit would be the least.

PBGC regulation 29 C.F.R. § 4044.13 further defines the requirements for a benefit to be in PC3.

**Issue 1: Whether PBGC correctly concluded that PC3 benefits do not include benefit increases resulting from: (1) the increased Internal Revenue Code ("IRC") § 401(a)(17) compensation limit that was enacted into law in June 2001; and (2) cost-of-living adjustments ("COLAs") to the IRC § 401(a)(17) limit for the years 2004 and 2005. AB at 6-13.**

IRC § 401(a)(17) limits the annual compensation that a defined benefit plan may "take into account" in determining pension benefits. The Economic Growth and Tax Relief Reconciliation Act of 2001 ("EGTRRA") enacted on June 7, 2001, increased the IRC § 401(a)(17) compensation cap to an annual amount of \$200,000 and provided for COLAs to the \$200,000 cap in future years.<sup>28</sup>

PBGC did not apply EGTRRA's increased compensation cap and subsequent COLAs in determining appellants' PC3 benefit amounts because, under the Pilots Plan's provisions, the increases were not in effect (i.e., payable) during the entire 5-year period before the Plan terminated.<sup>29</sup>

### **The Appeal.**

The Appeal asserts that PBGC should have included the benefit increases resulting from EGTRRA's \$200,000 compensation cap in PC3 because the increased cap was incorporated into

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<sup>28</sup> Pub. L. No. 107-16, § 611(c)(1), 115 Stat. 38, 97 (2001).

<sup>29</sup> Because the increase was not effective until July 1, 2002, any pilot who terminated Delta employment before that date would have compensation capped by the lower IRC § 401(a)(17) limit in effect before EGTRRA's enactment.

the Pilots Plan's provisions more than 5 years before the Pilots Plan terminated (i.e., before September 2, 2001). AB at 6-13. The Appeal disagrees with PBGC's conclusion that a benefit increase does not go into effect for PC3 purposes until the increase first becomes operative or receivable. AB at 10-11. The Appeal further claims that PBGC improperly excluded from PC3 the IRC § 401(a)(17) limit COLAs that went into effect in 2004 and 2005. AB at 12-13.

### **Our Conclusions.**

The Board decided, based on ERISA and PBGC regulations, that PBGC properly determined PC3 benefits using the lower, pre-EGTRRA compensation cap that was in effect at the start of the 5-year period before the Pilots Plan terminated.<sup>30</sup> The Board also decided that PBGC correctly excluded from PC3 the 2004 and 2005 COLAs to the IRC § 401(a)(17) limit.

### **Explanation of Board's Decision on Issue #1.**

#### **A. Background**

##### **1. The IRC § 401(a)(17) limit**

Congress initially established the IRC § 401(a)(17) limit through enactment of the Tax Reform Act of 1986 ("TRA '86").<sup>31</sup> Later, through the Omnibus Budget Reconciliation Act of 1993 ("OBRA '93"), Congress reduced the IRC § 401(a)(17) limit.<sup>32</sup> Approximately 8 years after OBRA '93's enactment, Congress increased the IRC § 401(a)(17) limit by enacting EGTRRA.

After the EGTRRA amendments, IRC § 401(a)(17)(A) provided that a pension plan could not be tax-qualified unless "the annual compensation of each employee taken into account under the plan for any year does not exceed \$200,000." As in the earlier statutory provisions, EGTRRA provided that the \$200,000 limit would be adjusted annually "for increases in the cost-of-living."<sup>33</sup>

For the Pilots Plan, EGTRRA's increase to the IRC § 401(a)(17) limit went into effect on July 1, 2002, which was approximately 4 years and 3 months before the Pilots Plan terminated.

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<sup>30</sup> Prior to EGTRRA's enactment, a \$170,000 annual cap applied to a pilot's earnings for the years 2000 and 2001. Also, under pre-EGTRRA law, the IRC § 401(a)(17) limits were lower than \$170,000 for earnings in the years 1994 through 1999.

<sup>31</sup> Pub. L. No. 99-514, 100 Stat. 2085 (1986). TRA '86 provided for an initial annual compensation limit of \$200,000 in 1989, plus COLAs for subsequent plan years.

<sup>32</sup> Pub. L. No. 103-66, 107 Stat. 312 (1993). Although OBRA '93 generally was effective in 1994, certain collectively bargained plans were allowed to postpone the effective date of the OBRA '93 change until as late as the start of the 1997 plan year.

<sup>33</sup> See IRC § 401(a)(17)(B).

EGTRRA's effective date is set forth in EGTRRA § 611(i), which provides that the amended IRC § 401(a)(17) limit "shall apply to [plan] years beginning after December 31, 2001." Since the plan year for the Pilots Plan began on July 1 and ended on June 30, EGTRRA's \$200,000 limit went into effect on July 1, 2002 (i.e., the first day of the plan year beginning after December 31, 2001).<sup>34</sup>

Due to EGTRRA's enactment and the COLA increases that occurred under OBRA '93 and EGTRRA, the IRC § 401(a)(17) compensation cap increased substantially between 1994 and the Pilots Plan's termination in 2006. The IRC § 401(a)(17) limits in effect for those years are as follows:

YEAR	AMOUNT
1994	\$150,000
1995	\$150,000
1996	\$150,000
1997	\$160,000
1998	\$160,000
1999	\$160,000
2000	\$170,000
2001	\$170,000
2002	\$200,000
2003	\$200,000
2004	\$205,000
2005	\$210,000
2006	\$220,000

## 2. The Pilots Plan's provisions

Benefits under the Pilots Plan are calculated using one of two formulas.<sup>35</sup> All pilots are eligible to have their benefit calculated under the "Final Average Earnings" ("FAE") formula. Certain pilots are also eligible to have their benefit calculated under an alternative "Minimum Benefit" formula, if the resulting benefit is higher than their benefit under the FAE formula. Both formulas contain an earnings component.<sup>36</sup>

<sup>34</sup> Section 1.27 of the Plan defines "Plan Year" as the "Company's fiscal year ending each June 30."

<sup>35</sup> See Plan § 1.18 (definition of "Formula Benefit"), § 5.01 (amount of normal retirement benefit), and § 8.02 (the Minimum Benefit formula).

<sup>36</sup> *Id.* The Minimum Benefit formula is discussed in detail under Issue #7.

The IRC § 401(a)(17) limit, which caps the amount of earnings a plan may use to calculate benefits under a tax-qualified plan, applies to both of the Pilots Plan's benefit formulas because, as stated above, both formulas contain an earnings component.

The applicable IRC § 401(a)(17) limits were incorporated into the Pilots Plan before and after EGTRRA's June 7, 2001 enactment through the following:<sup>37</sup>

- Section 1.12 of the 1996 Restatement provided that, effective July 1, 1996, "the Plan must limit Earnings during a Plan Year (including Plan Years before and after July 1, 1996) to \$150,000, as adjusted for the cost-of-living in accordance with Section 401(a)(17)(B) of the Code."
- On June 21, 2001 (2 weeks after EGTRRA's enactment), Delta entered into a collective bargaining agreement with ALPA called the "Pilot Working Agreement" ("PWA"), which provided for the EGTRRA increase. With respect to the IRC § 401(a)(17) limits, Section 26(G) of the PWA states in pertinent part:

If Internal Revenue Code Sections 401(a)(17), 415(b), and 415(c) (the "Qualified Plan Limits") are amended to increase the limitations therein, then any such increase will be effective for the [Pilots Plan] . . . as of the earliest date that the increase . . . could have become legally effective for that Plan, had that Plan not been collectively bargained . . . .

Because the Plan had a plan year beginning on July 1 and EGTRRA's amendment of the IRC § 401(a)(17) limit applies to "[plan] years beginning after December 31, 2001," the "earliest" effective date for the EGTRRA increase to the IRC § 401(a)(17) limit is July 1, 2002 for the Pilots Plan. Accordingly, the PWA provides that the increased IRC § 401(a)(17) limit for the Pilots Plan was effective on July 1, 2002.

- On July 27, 2003 (approximately 3 years and 2 months before DOPT), Delta adopted the Fourth Amendment, which incorporated EGTRRA's IRC § 401(a)(17) limit into the Plan's formal document. The Fourth Amendment provides that the "Earnings taken into account in determining benefit accruals of an Employee in any Plan Year beginning after June 30, 2002 shall not exceed \$200,000, as adjusted for cost-of-living increases in accordance with Section 401(a)(17)(B) of the Code."<sup>38</sup>

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<sup>37</sup> The Pilots Plan's provisions, both before and after EGTRRA, contain a special rule that applies to pilots who have pre-1996 earnings that are limited by the more generous \$200,000 cap (plus COLAs) in effect prior to OBRA '93. The Appeal does not address this special rule, and we do not explain it further in this decision. Instead, this decision (including the examples we present in Appendix A) explains how Delta and PBGC determined benefits under the much more common situation where the pilot's benefit under the generally-applicable rule exceeds the pilot's benefit under the special rule.

<sup>38</sup> Fourth Amendment at ¶ 2.

## **B. Discussion**

It is undisputed that Delta, through the PWA and Fourth Amendment, increased benefits under the Pilots Plan by amending its compensation cap following the June 7, 2001 enactment of EGTRRA. We use the term “Amended Compensation Cap” to refer to the increased compensation cap that was incorporated into the Pilots Plan’s provisions following EGTRRA’s enactment.

PBGC concluded that PWA § 26(G), which was adopted more than five years before the Pilots Plan terminated, should be treated as a Plan amendment.<sup>39</sup> The Appeal does not dispute, and the Appeals Board accepts, this conclusion.

The Board further found that, although the Fourth Amendment to the 1996 Restatement is more detailed than PWA § 26(G), there is no conflict between the two provisions concerning how the IRC § 401(a)(17) limits are to be applied.

The disputed question in Issue #1 is whether PBGC correctly determined that the benefit increases resulting from the Amended Compensation Cap are not in PC3. For the reasons given below, the Appeals Board decided that appellants impacted by the IRC § 401(a)(17) limit are not entitled to benefit increases in PC3.

### **1. PBGC correctly determined that the Amended Compensation Cap went into effect less than five years before the Pilots Plan terminated**

ERISA provides that there are two requirements for a benefit to be in PC3. The first is that the participant must have either retired or been eligible to retire at least three years before the plan’s termination date.<sup>40</sup> The second requirement – which is crucial for Issue #1 – is that the benefit amount in PC3 is based on the plan provisions “in effect” during the five years before the plan’s termination date “under which such benefit would be the least.”<sup>41</sup>

PBGC interprets this second requirement as providing that a benefit increase cannot be “in effect” for purposes of PC3 before the date on which the increase becomes operative. PBGC applies this rule even if the plan provision that provided for the increase has an earlier “stated” effective date. PBGC’s longstanding interpretation of ERISA’s PC3 requirements is based on its PC3 regulation, which provides:

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<sup>39</sup> See January 25, 2007 Memorandum from J. Armbruster and J. Krettek to S. Strassman and L. Burke Lee (the “2007 Legal Memorandum”) at 5, which you provided as Appeal Exhibit 20.

<sup>40</sup> ERISA § 4044(a)(3). This decision refers to the start date of this 3-year period as “DOPT-3.”

<sup>41</sup> *Id.* This decision refers to the start date of this 5-year period as “DOPT-5.”

- Benefit increases that “were effective *throughout* the 5-year period ending on the termination date . . . shall be included in determining the priority category 3 benefit.”<sup>42</sup>
- The PC3 benefit amount is limited to “the lowest annuity benefit *payable* under the plan provisions at any time during the 5-year period ending on the termination date.”<sup>43</sup>

Thus, if a benefit increase does not go into effect (i.e., is not payable) until after DOPT-5 and if a participant’s payable PC3 benefit amount would be lower based on the plan provisions that were in effect before the increase, then the increase is not included in the participant’s PC3 benefit.

PBGC correctly applied its PC3 regulation when it determined the effective date of the benefit increases under the Pilots Plan’s Amended Compensation Cap. Delta increased benefits under the Pilots Plan by incorporating EGTRRA’s \$200,000 limit for purposes of “determining benefit accruals of an Employee in any Plan Year beginning after June 30, 2002.”<sup>44</sup> The operative date of the increase (July 1, 2002) is later than both the PWA’s adoption date (June 21, 2001) and the stated effective date of the pension provisions in Section 26(G) of the PWA (September 1, 2001).<sup>45</sup> Thus, PBGC correctly concluded that benefit increases based on the Amended Compensation Cap went into effect on July 1, 2002, which was after the start of the 5-year period that ended on the Pilots Plan’s DOPT.

In claiming that the IRC § 401(a)(17) limit increases under EGTRRA should be in PC3, the Appeal focuses on the stated effective date in the PWA. Specifically, the Appeal states that PBGC should determine PC3 benefit amounts based on “when the provisions of the plan are in effect – not when the benefit itself was first operative or receivable.” AB at 10-11.

The Appeals Board decided that the Appeal presents no basis for changing PBGC’s longstanding position concerning how PC3 benefit amounts are determined. In the US Airways Decision, the Appeals Board affirmed PBGC’s conclusion that the benefit increase at issue in that case is not in PC3 because the “operative” date of the increase was less than five years

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<sup>42</sup> 29 C.F.R. § 4044.13(a) (emphasis added).

<sup>43</sup> 29 C.F.R. § 4044.13(b)(3) (emphasis added).

<sup>44</sup> Fourth Amendment at ¶ 2.

<sup>45</sup> You state, at AB 10, that PBGC incorrectly “equated the effective date of the EGTRRA *Amendment* with the earliest date, under *EGTRRA itself*, that the increased § 401(a)(17) limit could apply” (emphasis in original).

The Board found that PBGC applied the correct effective date in determining PC3 benefits. PBGC’s conclusion that the IRC § 401(a)(17) limit increases are not in PC3 is based on when, under the Pilots Plan’s provisions, the increases first could be applied in determining a retiree’s benefit. That date, July 1, 2002, also was the statutory effective date under EGTRRA for the Pilots Plan. Accordingly, PBGC appropriately made its PC3 determinations based on the dates when the IRC § 401(a)(17) limit increases went into effect under the Pilots Plan’s provisions, which coincided with EGTRRA’s effective date for the Pilots Plan.

before plan termination.<sup>46</sup> The District Court in *Davis* upheld PBGC's interpretation of ERISA's PC3 provisions as a "permissible construction of the statute."<sup>47</sup> The Appeals Board rejected the PC3 interpretation advanced in the Appeal for the same reasons stated in the US Airways Decision and in *Davis*.

## **2. The "lowest annuity benefit payable" in the 5-year period before the Pilots Plan's termination does not include the Amended Compensation Cap increases**

ERISA § 4044(a)(3) and PBGC regulation 29 C.F.R. § 4044.13(b)(3) provide that the PC3 benefit amount is limited to the lowest annuity benefit payable under the plan provisions at any time during the 5-year period ending on the termination date. The Appeals Board found that PBGC correctly determined the "lowest annuity benefit" for PC3 purposes when it applied the IRC § 401(a)(17) limits to a pilot's earnings.

The Board's finding is based on the Pilots Plan's terms and its practice. As previously stated, the PWA and the Fourth Amendment incorporate EGTRRA's \$200,000 limit for purposes of "determining benefit accruals of an Employee in any Plan Year beginning after June 30, 2002." Delta, in accordance with this Pilots Plan provision, applied EGTRRA's \$200,000 limit if the pilot retired or separated from service after July 1, 2002.<sup>48</sup> Delta did not apply the \$200,000 limit, however, if the pilot's benefit accruals ended before July 1, 2002 due to the pilot's retirement or separation from Delta employment.

Delta's practice in applying the IRC § 401(a)(17) limits, which the Board found to be consistent with Plan's terms, is explained in detail in Appendix A to this decision. The examples presented in Appendix A, which are for pilots who retired on different dates within the 5-year period before Plan termination, show:

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<sup>46</sup> The plan amendment at issue in the US Airways Pilots Plan Appeal had both an adoption date and a "stated" effective date more than 5 years before plan termination. A US Airways pilot, however, could not retire and receive the increased benefit until May 1, 1998, which was less than 5 years before the US Airways Pilots Plan terminated (March 31, 2003). Based on those facts, the Appeals Board concluded that the increases at issue for US Airways pilots were not in PC3. See US Airways Decision at 8-10 (Enclosure 3). The Appeals Board found no meaningful distinction between the facts relevant to Issue #1 of the Appeal and the facts decided by the Board in the US Airways Decision.

<sup>47</sup> *Davis*, 864 F.Supp.2d at 157; see also *Davis v. PBGC*, 571 F.3d 1288, 1292-93 (D.C. Cir. Jul. 10, 2009) (denial of preliminary injunction).

<sup>48</sup> Section 1.30 of the 1996 Restatement defines "Retirement Date" as "the first day of the month coincident with or immediately following the date the Participant actually ceases employment for Early Retirement, Normal Retirement or Deferred Retirement, whichever is applicable." Under the Pilots Plan's practice, a pilot could not simultaneously earn benefit accruals and retire on the first day of the month. Thus, for example: (1) if the pilot's last date of active Delta employment is on June 30<sup>th</sup>, the Retirement Date is July 1<sup>st</sup>; and (2) if the pilot's last date of active Delta employment is on July 1<sup>st</sup>, the Retirement Date is August 1<sup>st</sup>.

- If the pilot retired on or before July 1, 2002, Delta determined the Pilots Plan benefit using the lower IRC § 401(a)(17) limits under OBRA '93 that are referenced in the 1996 Restatement.
- For retirements after July 1, 2002, Delta applied the higher IRC § 401(a)(17) limit under EGTRRA, in accordance with the PWA and the Fourth Amendment.

Thus, for retirements during the first 9 months of the 5-year period before DOPT (i.e., between October 1, 2001 and July 1, 2002), Delta computed Pilots Plan benefits based on the lower IRC § 401(a)(17) limits under OBRA '93, as was required under the Plan's terms.

As illustrated by the examples in Appendix A, the Pilots Plan provisions in effect at DOPT-5, rather than the Amended Compensation Cap, provide lower benefits for pilots who were actively employed five years before Plan termination and whose earnings are impacted by the IRC § 401(a)(17) limits.<sup>49</sup> PBGC accordingly complied with ERISA and PBGC regulations when it applied the Pilots Plan provisions in effect at DOPT-5 to determine the lowest benefit amounts for PC3 purposes.

The Appeal contends that, even under the PBGC's "effective date criteria" for PC3, PBGC incorrectly excluded the increased IRC § 401(a)(17) limit from PC3. AB at 11-12. In making this assertion, the Appeal disregards the above analysis and, instead, refers to the Pilots Plan provisions that apply to pilots who retired after July 1, 2002.<sup>50</sup> As explained above, PBGC correctly concluded that the lowest benefit for PC3 purposes is the one without the EGTRRA increase, notwithstanding that the increase would be payable under Plan provisions to a pilot who retired after July 1, 2002.

### **3. PBGC did not disregard IRS guidance when it concluded that the Amended Compensation Cap increases were not in PC3**

The Appeal contends that PBGC improperly excluded benefit increases under the Amended Compensation Cap from PC3 because, under applicable IRS Guidance, the amended \$200,000

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<sup>49</sup> The Plan provisions in effect at DOPT-5 ordinarily produce lower benefits for pilots affected by the IRC § 401(a)(17) limits because: (1) earnings are a component of the Pilots Plan's benefit formulas; and (2) the lower compensation cap in effect at DOPT-5 reduces the earnings that can be used in the pension calculation. The DOPT-5 provisions ordinarily produce a smaller benefit regardless of whether the pilot's benefit is determined under the FAE formula or Minimum Benefit formula. Please note that PBGC calculated the pilot's PC3 benefit amounts under both the FAE formula and Minimum Benefit formula and included in PC3 the larger of the two amounts. See discussion under Issue #7.

<sup>50</sup> The Appeal correctly states that for post-July 1, 2002 retirees, the Pilots Plan applied the \$200,000 EGTRRA limit retroactively to pre-2002 compensation in calculating benefits. The Appeal also correctly states that, for many pilots eligible for PC3, the 36-month period that comprises their highest earnings will include a plan year that is prior to EGTRRA's enactment. AB at 12. The Appeal, however, does not take into account how the Pilots Plan's provisions apply to pilots who retired on or before July 1, 2002; for these pilots, there is no EGTRRA increase to the IRC § 401(a)(17) limit. See the 1996 Restatement § 1.12 and Fourth Amendment at ¶ 2.

limit could apply to compensation that a participant earned in plan years beginning before January 1, 2002.<sup>51</sup> AB at 10-12.

There is no conflict between IRS Notice 2001-56 and the PBGC's conclusion, based on the Pilots Plan's provisions, that the Amended Compensation Cap increases are not in PC3. IRS Notice 2001-56 provides that a pension plan could choose among several alternative approaches in implementing the EGTRRA amendments.<sup>52</sup> The approach adopted by Delta, under which the \$200,000 EGTRRA limit applied only to participants who retired after July 1, 2002, is one of the permitted methods of compliance with IRS Notice 2001-56. Even though Delta possibly could have adopted a different approach under IRS Notice 2001-56, PBGC correctly concluded that the \$200,000 EGTRRA increase is not in PC3 based on the Plan provisions that Delta actually adopted. For this reason, the Board rejected your Issue #1 contentions based on IRS Notice 2001-56.

#### **4. PBGC correctly excluded from PC3 the 2004 and 2005 COLAs to the IRC § 401(a)(17) limit**

The Pilots Plan's provisions expressly incorporated the IRC § 401(a)(17) limit COLAs under EGTRRA.<sup>53</sup> The first COLA increase to EGTRRA's \$200,000 limit occurred in 2004, when the limit increased to \$205,000.<sup>54</sup> In 2005, the limit increased to \$210,000.

When PBGC calculated benefits in PC3, it excluded benefit increases under the IRC § 401(a)(17) limit COLAs for 2004 and 2005. As is the case with EGTRRA's initial \$200,000 limit, PBGC concluded that each COLA increase to the IRC § 401(a)(17) limit was in effect for purposes of PC3 on the date when the COLA increase became operative, i.e. payable. PBGC further concluded that the lowest benefit for PC3 purposes is the one without the 2004 and 2005 IRC § 401(a)(17) limit COLAs.

The Appeal contends that PBGC, in excluding the 2004 and 2005 COLA increases from PC3, erroneously applied the "automatic benefit increases" provision in PBGC's regulation 29

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<sup>51</sup> The Appeal quotes the following language from IRS Notice 2001-56, 2001-2 C.B. 277:

In the case of a plan that uses annual compensation for periods prior to the first plan year beginning on or after January 1, 2002, to determine accruals or allocations for a plan year beginning on or after January 1, 2002, the plan is permitted to provide that the \$200,000 compensation limit applies to annual compensation for such periods in determining such accruals or allocations.

<sup>52</sup> IRS Notice 2001-56 states that a pension plan generally "is not required to implement the EGTRRA increase in the compensation limit under § 401(a)(17) of the Code in its benefit formula." A pension plan also has the option of providing "any other compensation limit that is less than the compensation limit as amended by EGTRRA."

<sup>53</sup> Fourth Amendment at ¶ 2.

<sup>54</sup> In 2002 and 2003, there were no COLA increases to EGTRRA's initial \$200,000 limit.

C.F.R. § 4044.13(b)(5). AB at 12-13. The Appeal notes that, under 29 C.F.R. § 4044.13(b)(5), only automatic benefit increases scheduled during the fourth and fifth years preceding plan termination may be included in PC3.<sup>55</sup> AB at 12-13. The Appeal takes the position that the 2004 and 2005 COLAs to the IRC § 401(a)(17) limit must be included in PC3 because they are “Congressionally imposed cost-of-living adjustments,” rather than “automatic increases in the benefit formula.” AB at 13.<sup>56</sup>

The Appeal’s position concerning the COLA increases to the IRC § 401(a)(17) limit is without merit. Pension plans were not required by EGTRRA, or by any other legislation, to increase benefits based on the IRC § 401(a)(17) limit COLAs. Rather, EGTRRA provided pension plan sponsors with the opportunity to adopt plan amendments that would allow the annual compensation cap to increase based upon the IRC § 401(a)(17) limit COLAs. If the \$200,000 limit and subsequent COLAs had not been incorporated into the Pilots Plan’s provisions, the Pilots Plan could not have paid such increases because fiduciaries are required to administer an ERISA plan “in accordance with the documents and instruments governing the plan.”<sup>57</sup>

As authorized by EGTRRA, Delta changed the Pilots Plan’s provisions, through the PWA and Fourth Amendment, by incorporating by reference the COLAs permitted under EGTRRA. Thus, the IRC § 401(a)(17) limit COLAs became part of the Pilots Plan’s benefit formula through the Plan’s usual amendment procedures. The Appeals Board found no reason to treat benefit increases based on the IRC § 401(a)(17) limit COLAs differently from benefit increases that occur under other types of plan amendments.<sup>58</sup>

The “automatic benefit increases” provision in 29 C.F.R. § 4044.13(b)(5) allows PBGC to include in PC3 certain benefit increases that would otherwise be excluded by the PC3

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<sup>55</sup> Even if an automatic benefit increase is scheduled to go into effect during the fourth and fifth years preceding plan termination, the increase must meet additional requirements, which are specified in 29 C.F.R. § 4044.13(b)(5), in order to be included in PC3.

<sup>56</sup> The Appeal makes the following arguments in asserting that the IRC § 401(a)(17) limit COLAs are not automatic benefit increases: (1) the COLAs are not part of the benefit formula because the COLAs are “contained in an entirely separate section” of the Pilots Plan document from the Plan’s “benefit formula;” (2) “far from increasing benefits, the § 401(a)(17) limit operates to restrict benefits by capping the amount of compensation that can be used to determine a participant’s retirement benefit, with the yearly COLAs merely easing that limitation;” and (3) “even if the § 401(a)(17) COLAs could be construed as conferring a benefit ‘increase,’ any such increase is certainly not ‘automatic’: if a participant earns an amount that is less than or equal to the § 401(a)(17) limit, any subsequent COLA does not affect that participant’s benefits whatsoever, let alone ‘increases’ their benefit.” *Id.*

<sup>57</sup> ERISA § 404(a)(1)(D).

<sup>58</sup> See US Airways Decision at 21-22 (Appeals Board rejected similar PC3 argument concerning COLA increases under IRC § 415(b)); see also *Davis*, 864 F.Supp.2d at 157-158 (court upheld PBGC’s exclusion from PC3 of IRC § 415(b) COLA increases that went into effect after DOPT-3).

regulation.<sup>59</sup> As you note in the Appeal, one of the requirements in 29 C.F.R. § 4044.13(b)(5) for including an automatic benefit increase in PC3 is that the increase is “scheduled” to go into effect during the fourth and fifth years preceding plan termination. In the case of the 2004 and 2005 COLAs, the increases were not scheduled to go into effect – and did not actually go into effect – until the third and the second year before the Pilots Plan’s DOPT. PBGC thus correctly concluded that the 2004 and 2005 COLAs to the IRC § 401(a)(17) limit do not qualify for inclusion in PC3 under 29 C.F.R. § 4044.13(b)(5).<sup>60</sup>

For the above reasons, the Appeals Board affirmed PBGC’s determination that benefit increases resulting from the Amended Compensation Cap and the 2004 and 2005 IRC § 401(a)(17) limit COLAs are excluded from PC3. In so ruling, the Board concluded that PBGC properly applied the requirements in ERISA and in PBGC regulations, including PBGC’s automatic benefit increase provision in 29 C.F.R. § 4044.13(b)(5).

**Issue 2: Whether PBGC correctly concluded that PC3 benefits do not include benefit increases for “retired pilots” resulting from: (1) the increased IRC § 415(b) limit on benefit payments that was enacted into law in June 2001; and (2) the IRC § 415(b) COLAs for the years 2004, 2005, and 2006. AB at 14-17.**

IRC § 415(b) limits the benefit payments that a tax-qualified defined benefit pension plan can make with respect to an individual participant in a given year. EGTRRA increased the IRC § 415(b) limit to \$160,000 (effective July 1, 2001 for the Pilots Plan) and provided for COLA increases to the \$160,000 limit in future years.<sup>61</sup>

PBGC concluded that PWA § 26(G) fully incorporated EGTRRA’s increased IRC § 415(b) limits into the Pilots Plan more than 5 years before DOPT for Delta’s “active pilots” only. For purposes of this issue, “active pilots” are Delta pilots (or former pilots) who had not retired or separated from service prior to the PWA’s July 1, 2001 effective date. PBGC applied EGTRRA’s \$160,000 IRC § 415(b) limit in calculating the active pilots’ PC3 benefits.

PBGC did not apply EGTRRA’s \$160,000 IRC § 415(b) limit when it calculated PC3 benefits for Delta pilots who retired or separated from service before July 1, 2001 (the “retired

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<sup>59</sup> See 46 Fed. Reg. 9480, 9484 (Jan. 28, 1981) (discussion of “automatic benefit increases” in the preamble to PBGC’s final Asset Allocation regulation).

<sup>60</sup> The Board further decided that the 2004 and 2005 COLAs to the IRC § 401(a)(17) limit cannot be included in PC3 for a second reason. PBGC’s PC3 regulation states that an automatic benefit increase cannot be included in PC3 unless a plan provision adopted and effective on or before DOPT-5 “provided for automatic increases in the benefit formula for both active participants and those in pay status or for participants in pay status only.” See 29 C.F.R. § 4044.13(b)(5). Benefit increases resulting from the 2004 and 2005 COLAs to the IRC § 401(a)(17) limit do not meet the above-stated requirement because, under the Pilots Plan’s provisions, a COLA increase to the IRC § 401(a)(17) limit is provided for active participants only, i.e., participants who accrued benefits after the COLA’s effective date.

<sup>61</sup> Pub. L. No. 107-16, §§ 611(a), 611(g), and 611(i)(2), 115 Stat. 38, 96-100 (2001).

pilots”). Instead, PBGC applied the lower IRC § 415(b) limit in effect before EGTRRA. PBGC concluded that the retired pilots could not receive PC3 benefits based on the greater EGTRRA IRC § 415(b) limit because: (1) PWA § 26(G) did not apply to their benefits; and (2) although Delta adopted a Plan amendment after DOPT-5 that provided the retired pilots with the EGTRRA increases, the adoption date was too late for the increases to be included in PC3.

PBGC also did not include in PC3 the benefit increases resulting from the 2004, 2005 and 2006 COLAs to the IRC § 415(b) limits for both the active pilots and the retired pilots, for reasons explained below.

### **The Appeal.**

The Appeal contends that PBGC erred in not applying EGTRRA’s \$160,000 IRC § 415(b) limit in determining PC3 benefits for the retired pilots. AB at 14-17. You assert that the retired pilots should be treated similarly to the active pilots who are receiving PC3 benefits based on the \$160,000 § 415(b) limit. *Id.* You further claim that PBGC improperly excluded from PC3 the IRC § 415(b) limit COLAs for the years 2004, 2005, and 2006. AB at 17.

### **Our Conclusions.**

The Appeals Board decided, based on ERISA, PBGC regulations, and the Pilots Plan’s provisions, that PBGC applied the appropriate IRC § 415(b) limits when it determined PC3 benefits for the retired pilots and for the active pilots. The Board also decided that, for both groups, PBGC correctly excluded from PC3 benefits the 2004, 2005, and 2006 COLA increases to the IRC § 415(b) limit.

### **Explanation of Board’s Decision on Issue #2.**

#### **A. Background**

##### **1. The IRC § 415(b) limit**

IRC § 415(a) provides, generally, that a trust that is part of a pension plan shall not constitute a tax-qualified trust if “in the case of a defined benefit plan, the plan provides for the payment of benefits with respect to a participant which exceed the limitation of subsection (b) . . . .” Thus, in order to meet the requirements for a tax-qualified pension plan under the IRC, a plan must cap pension payments if a participant’s accrued benefit exceeds the IRC § 415(b) limit.

IRC § 415(b), as in effect in 2001 prior to passage of EGTRRA, provided that the highest annual benefit payable under a defined benefit plan was the *lesser* of \$90,000 or 100% of the

participant's compensation.<sup>62</sup> Section 415(d) further provided for COLAs to the 415(b)(1)(A) amounts.

When Congress passed EGTRRA on June 7, 2001, it increased the IRC § 415(b) limit to an initial amount of \$160,000.<sup>63</sup> The \$160,000 amount reflected a "base period" of the calendar quarter beginning July 1, 2001, and EGTRRA provided that adjustments based on COLAs would occur thereafter.<sup>64</sup> The IRC § 415(b)(1) limits in effect for the years 2000 through 2006 are as follows:<sup>65</sup>

YEAR	AMOUNT
2000	\$135,000
2001	\$140,000
2002	\$160,000
2003	\$160,000
2004	\$165,000
2005	\$170,000
2006	\$175,000

EGTRRA contains a special effective date provision, which applies only to its amendment of the IRC § 415(b) limit. Under this special provision, the IRC § 415(b) limit amendment applies to plan "years *ending after* December 31, 2001."<sup>66</sup> This contrasts with EGTRRA's general effective date for its pension amendments, which is for plan "years *beginning after* December 31, 2001."<sup>67</sup> Thus, for plans like the Pilots Plan where the Plan Year is different than the calendar year, the EGTRRA effective date is one year earlier for the IRC § 415(b) limit than for the IRC § 401(a)(17) limit (the limit discussed in Issue #1).

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<sup>62</sup> The \$90,000 amount cited above reflected a "base period" of the calendar quarter beginning October 1, 1986.

<sup>63</sup> EGTRRA § 611(a)(1).

<sup>64</sup> Additionally, IRC § 415(b)(2), which defines the term "annual benefit," contains a number of rules for determining the IRC § 415(b) amount (with those rules also being changed several times through legislation). These include requirements that the IRC § 415(b)(1)(A) limit be actuarially adjusted: (1) for benefits payable in forms other than as a straight life annuity; and (2) when benefit payments begin before age 62, or after age 65. IRC § 415(b)(3) through (b)(11) contain additional rules for determining the IRC § 415 limits for defined benefit plans, including (in IRC § 415(b)(9)) a special rule for commercial airline pilots. *See also* Treasury Decision 9319, 72 Fed. Reg. 16,878 (April 5, 2007) (final IRS regulation concerning IRC § 415 limits).

<sup>65</sup> *See* IRS COLA Increases Table, *available at* [http://www.irs.gov/pub/irs-tege/cola\\_table.pdf](http://www.irs.gov/pub/irs-tege/cola_table.pdf).

<sup>66</sup> EGTRRA § 611(i)(2) (emphasis added).

<sup>67</sup> EGTRRA § 611(i)(1) (emphasis added).

The plan year for the Pilots Plan runs from July 1 to June 30. As stated above, EGTRRA's IRC § 415(b) limit increases apply to plan years ending after December 31, 2001. The first Pilots Plan year ending after December 31, 2001 is the Plan year that starts on July 1, 2001 and ends on June 30, 2002. Accordingly, the statutory effective date of EGTRRA's IRC § 415(b) limit increases for the Pilots Plan is July 1, 2001. Thus, the statutory effective date of EGTRRA's IRC § 415(b) limit increases for the Pilots Plan (July 1, 2001) occurred more than five years before the Plan's September 2, 2006 DOPT.

## **2. Annual benefit caps under the Pilots Plan's formal documents and the PWA**

The IRC § 415(b) limit was incorporated into the Pilots Plan before and after EGTRRA's June 7, 2001 enactment through the following:

- Section 12.11(a)(i)(A) of the 1996 Restatement, which was in effect on the date of EGTRRA's enactment, states that the annual benefit "paid to or on behalf of a Participant shall not exceed . . . \$90,000," plus the (additional) annual COLAs determined by the Secretary of the Treasury under IRC § 415(d).
- As discussed under Issue #1, Delta and ALPA entered into a collective bargaining agreement, the PWA, on June 21, 2001, 2 weeks after EGTRRA's enactment. Section 26(G) of the PWA provides that, if the IRC § 415(b) limits "are amended to increase the limitations therein," any such increase will be effective for the Pilots Plan "as of the earliest date that the increase . . . could have become legally effective for that Plan, had that Plan not been collectively bargained." Delta adopted this PWA provision approximately two years before it incorporated EGTRRA's IRC § 415(b) limit into the Plan's formal document, which occurred through the Fourth Amendment.
- The formal Plan provision in effect after EGTRRA's enactment, the Fourth Amendment, states that the annual benefit "paid to or on behalf of a Participant shall not exceed . . . \$160,000," plus the (additional) annual COLAs determined by the Secretary of the Treasury under IRC § 415(d).<sup>68</sup>

The Fourth Amendment provides that, for the active pilots, the IRC § 415(b) increases were effective as of July 1, 2001 (the earliest effective date under EGTRRA). For the retired pilots, however, the Fourth Amendment provides that the IRC § 415(b) limit increases did not go into effect until July 1, 2002 (one year after the earliest effective date under EGTRRA).<sup>69</sup> As

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<sup>68</sup> Fourth Amendment at ¶ 5.

<sup>69</sup> To be precise, the Fourth Amendment provides that benefit increases resulting from EGTRRA's amendment of the IRC § 415(b) limit are effective on different dates depending on the employee's Annuity Starting Date ("ASD"). The IRC § 415(b) limit increases were effective July 1, 2001 for employees with ASDs "on or after July 1, 2001" and were effective on July 1, 2002 for employees with ASDs "before July 1, 2001." The Pilots Plan defines "Annuity Starting Date" as "the first day of the first period for which a retirement benefit is paid as an annuity." The 1996 Restatement § 1.05. Thus, a pilot's ASD is on or after his or her retirement date.

discussed later, the Fourth Amendment's establishment of different effective dates for the two groups of participants is significant with respect to the Board's resolution of Issue #2.

### **3. The Pilots Plan's practice**

Although many retired and active Delta pilots did not have Pilots Plan benefits that exceeded the IRC § 415(b) limit, we found examples where the IRC § 415(b) limit impacted pilots' benefit amounts. Based on these examples, we found that the Pilots Plan's practice was as follows:

- Retired pilots affected by the IRC § 415(b) limit. On July 1, 2001, Delta increased Pilots Plan payments to retired pilots based on the pre-EGTRRA IRC § 415(b) limit. Accordingly, a retired pilot who received \$11,250.00 per month before July 1, 2001 (based on the 2000 IRC § 415(b) annual limit of \$135,000) had his Pilots Plan payments increased to \$11,666.67 starting on July 1, 2001 (based on the 2001 IRC § 415(b) annual limit of \$140,000) if he was entitled to the larger amount under the Pilots Plan's benefit formulas. The retired pilot described above could not begin receiving Pilots Plan payments based on the \$160,000 IRC § 415(b) limit under EGTRRA (i.e., \$13,333.33 per month) until July 1, 2002.
- Active pilots affected by the IRC § 415(b) limit. A Delta pilot who was "active" on June 30, 2001 and afterwards decided to retire (i.e., had an ASD on or after July 1, 2001) received Pilots Plan payments starting on his retirement date that were capped by EGTRRA's \$160,000 limit. For example, a pilot who retired on July 1, 2001 would receive monthly Pilots Plan payments of \$13,333.33 (\$160,000 per year) starting on July 1, 2001, if he was entitled to that amount under the Pilots Plan's benefit formulas.

In 2003, the IRC § 415(b) limit remained at \$160,000. Due to COLAs, the annual IRC § 415(b) limit increased to \$165,000 in 2004, to \$170,000 in 2005, and to \$175,000 in 2006. For retirees, the Pilots Plan implemented these three COLA increases to the IRC § 415(b) limit at the beginning of each plan year (July 1).

## **B. Discussion**

### **1. A Pilots Plan amendment was necessary to implement the EGTRRA increases to the IRC § 415(b) limit**

As stated under Issue #1, ERISA and PBGC regulations provide that the benefit in PC3 is the benefit payable as of three years before the termination date "based on the provisions of the

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Significantly, the first available ASD for a participant who was an active Delta pilot on the PWA's adoption date (June 21, 2001) was July 1, 2001. Accordingly, a pilot who was active on the PWA's adoption date and retired with a July 1, 2001 ASD became entitled (based on the PWA and Fourth Amendment) to the increased IRC § 415(b) limit on July 1, 2001. As stated in the Fourth Amendment, a pilot with an ASD prior to July 1, 2001 could not receive benefit payments based on the increased IRC § 415(b) limit until July 1, 2002.

plan (as in effect during the 5-year period ending on such date) under which such benefit would be the least.”<sup>70</sup>

For the Pilots Plan, the statutory effective date for the EGTRRA increases to the IRC § 415(b) limit (July 1, 2001) was more than five years before DOPT (September 2, 2006). The EGTRRA increases to the IRC § 415(b) limit did not automatically become payable, however, on the statutory effective date.<sup>71</sup> Rather, Delta needed to adopt a Pilots Plan amendment in order for the EGTRRA increases to become payable to Plan participants.

A Pilots Plan amendment was necessary because, under the 1996 Restatement provision in effect before EGTRRA, annual payments were limited to \$90,000, adjusted “automatically for the cost-of-living for each calendar year pursuant to the regulations promulgated by the Secretary of the Treasury under section 415(d) of the Code.”<sup>72</sup> Thus, to increase the Plan’s payments based on EGTRRA’s \$160,000 limit, the Pilots Plan’s terms needed to be changed.

Because the Pilots Plan needed to be amended to incorporate EGTRRA’s increased IRC § 415(b) limits, a critical question under Issue #2 is whether the Pilots Plan was amended before DOPT-5 to provide for the increases. PBGC concluded: (1) PWA § 26(G) should be considered a Pilots Plan amendment, because it was a written instrument reflecting an agreement to amend the Plan and was signed by Delta; and (2) for participants covered by the PWA, benefit increases resulting from EGTRRA’s IRC § 415(b) limit of \$160,000 are in PC3 because the PWA was adopted in June 2001 and the \$160,000 limit was effective in July 2001, with both of those dates being more than five years before DOPT.<sup>73</sup>

PBGC further concluded that the \$160,000 limit should be applied only to the PC3 benefits of participants who had ASDs on or after July 1, 2001 (the active pilots). PBGC concluded that the EGTRRA increase was not in PC3 for participants with ASDs before July 1, 2001 (the retired

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<sup>70</sup> ERISA § 4044(a)(3); *see* 29 C.F.R. § 4044.13.

<sup>71</sup> While pension plans generally needed to be amended in order for EGTRRA’s improved IRC § 415(b) limit to go into effect, there is an exception if the pension plan had a pre-existing provision under which pension payments would increase automatically whenever the IRC § 415(b) limit was increased by legislation. *See* IRS Bulletin No. 2001-45, Q&A 2 (Nov. 5, 2001). The Pilots Plan did not have such a provision before EGTRRA was enacted. Therefore, Delta needed to amend the Plan to implement EGTRRA’s improved IRC § 415(b) limit. As stated above, the EGTRRA increases were incorporated into the Pilots Plan through the PWA and the Fourth Amendment.

We further observe that pension plans were not required to adopt the new 415(b) limit provided under EGTRRA. *See* 26 C.F.R. §§ 1.415(a)-1(d)(3)(v)(A), 1.415(d)-1(d); *see also* IRS Rev. Rul. 2001-51, Q&A 2-3, 2001-2 C.B. 427, 432-33 (explaining that EGTRRA did not require plans to increase plan benefits to the maximum permitted under IRC § 415(b); plans were permitted to continue applying the pre-EGTRRA limitations, including COLAs that would have been in effect if EGTRRA had not been enacted).

<sup>72</sup> The 1996 Restatement § 12.11(a)(i)(A).

<sup>73</sup> *See* 2007 Legal Memorandum at 4-5 (Appeal Exhibit 20).

pilots) because the retired pilots are not covered by PWA § 26(G) and they did not become entitled to the EGTRRA increases until after DOPT-5.<sup>74</sup>

The Appeal states that PBGC correctly determined that PWA § 26(G) should be “deemed” a Plan amendment that was “both adopted and effective prior to DOPT-5.” AB at 14. You disagree, however, with PBGC’s conclusion that the increased IRC § 415(b) limit under the PWA applied “only for those pilots who were active at the time the 2001 PWA was signed.” AB at 14; *see also* AB 15-17. For the reasons stated below, the Appeals Board agreed with PBGC’s interpretation of the PWA’s IRC § 415(b) limit provision.

**2. PBGC correctly concluded that PWA § 26(G) did not provide the retired pilots with increases to the IRC § 415(b) limit**

You maintain that the EGTRRA increases to the IRC § 415(b) limits, which were incorporated into the Plan through the PWA, should be included in PC3 because the PWA “amended the Plan for everyone, not just for the then-active pilots.” AB at 14. In advancing this position, you disagree with PBGC’s conclusion that PWA § 26(G) exclusively applies to the then-active pilots who were represented by ALPA in collective bargaining. AB at 15-16. Rather, you assert that “[n]othing in the actual language of § 26(G) can reasonably be read to support the PBGC’s inference that the Plan amendment applied only to certain participants.” AB at 15-16.<sup>75</sup>

The Appeals Board reviewed the PWA, the Fourth Amendment, and other applicable Pilots Plan provisions. The Board agreed with PBGC that PWA § 26(G) did not amend the Pilots Plan for retirees or pilots who had separated from service prior to the PWA’s adoption. The PWA’s “Scope” provision defines the “Pilot Working Agreement” as “the basic collective bargaining agreement between Delta Air Lines, Inc. and the air line pilots in the service of Delta Air Lines, Inc. as represented by the Air Line Pilots Association International, together with all effective amendments, supplemental agreements, Letters of agreement, and letters of understanding between the Company and the Association.”<sup>76</sup> The PWA also states that it “cover[s] the pilots in the employ of the Company.”<sup>77</sup> The Agreement further defines “Pilot” as “an employee of Delta Air Lines, Inc. whose name appears on the Delta Air Lines Pilots’ System Seniority List.”<sup>78</sup>

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<sup>74</sup> PBGC’s conclusions are set forth in the 2007 Legal Memorandum at 5-6 and in PBGC’s Actuarial Case Memo at 17-18.

<sup>75</sup> Your September 21, 2012 letter to the Appeals Board states in footnote 7: “Appellants note that the Fourth Amendment merely formalizes a long-standing requirement under the Plan, going back to at least 1991, that the Plan calculated and paid the maximum retirement benefits allowed under the IRC limits in effect in any given year as far back as 1985.”

<sup>76</sup> PWA §§ 1(B)(18), 2(A)(120).

<sup>77</sup> PWA § 1(A)(1).

<sup>78</sup> PWA § 2(A)(118).

These definitions demonstrate that the PWA is an agreement that governs the rights, terms, and conditions of employment of then-active Delta pilots.

Furthermore, as stated in the 2007 Legal Memorandum, the law does not presume that a collective bargaining agreement covers retired employees. To the contrary, the Supreme Court has found that, “[s]ince retirees are not members of the bargaining unit, the bargaining agent is under no statutory duty to represent them in negotiations with the employer.”<sup>79</sup> The Court acknowledged, however, that this does not preclude a bargaining unit from representing retirees if the employer agrees and the retirees assent.<sup>80</sup>

The above legal authority establishes that there can be no presumption that a collective bargaining agent represents retirees in negotiations or that a collective bargaining agreement covers them with respect to retirement benefits. If there is specific evidence establishing that a collective bargaining representative agreed to represent retirees’ interests with respect to a specific matter, there could be a basis for concluding that retirees are covered under a particular collective bargaining provision that is otherwise unclear concerning its scope. The Appeals Board found insufficient evidence to establish that ALPA was representing the interests of retired pilots when it negotiated PWA § 26(G).

As the 2007 Legal Memorandum concludes, the terms of the Fourth Amendment (which was adopted in 2003) further support the conclusion that PWA § 26(G) does not apply to the retired pilots. The Fourth Amendment explicitly provides for different effective dates for the IRC § 415(b) limit increase depending upon the ASD. For a participant who retired prior to July 1, 2001, the increase to \$160,000 was not effective until July 1, 2002.<sup>81</sup> In contrast, the increase to \$160,000 was effective on July 1, 2001 for those pilots with an ASD on or after that date. The Fourth Amendment is wholly consistent with the PWA only if we conclude that the PWA does not amend the Pilots Plan’s IRC § 415(b) benefit limit for retired pilots. Otherwise, there would be a clear conflict between the “earliest effective date” language in the PWA and the delayed effective date for the retired pilots in the Fourth Amendment. For all of the above reasons, the Appeals Board agreed with PBGC’s conclusion that PWA § 26(G) does not apply to the retired pilots.

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<sup>79</sup> *Allied Chemical & Alkali Workers of America v. Pittsburgh Plate Glass Co.*, 404 U.S. 157, 399 n.20 (1971); see also National Labor Relations Act, §§ 8(a)(1), 8(a)(5), 8(d) as amended, 29 U.S.C. §§ 158(a)(1), 158(a)(5), 158(d).

<sup>80</sup> *Allied Chemical*, 404 U.S. at 399 n.20; see also *Rosetto v. Pabst Brewing Co.*, 128 F.3d 538, 540-41 (7th Cir. 1997). In *Rosetto*, the court stated: “Although a union has no duty to represent retirees, and retirees need not submit to union representation, retirees are free to make a union their agent if they so choose. And, of course, retiree benefits are a permissive subject of bargaining – a union may bargain for retirees if the employer agrees.” 128 F.3d at 540-41.

<sup>81</sup> Fourth Amendment at ¶ 5.

### 3. Benefit Increases Resulting from EGTRRA's Increase of the IRC § 415(b) Limit to \$160,000 are not in PC3 for the Retired Pilots

PBGC regulations provide that, for PC3 purposes, “a plan or amendment is ‘in effect’ on the later of the date on which it is adopted or the date it becomes effective.”<sup>82</sup> Additionally, the regulations state that “[b]enefit increases that were effective throughout the 5-year period” are included in PC3.<sup>83</sup> Finally, the regulations provide that the amount in PC3 is limited to “the lowest annuity benefit *payable* under the plan provisions *at any time* during the 5-year period ending on the termination date.”<sup>84</sup>

Based on these regulatory provisions and the Pilots Plan's terms, PBGC correctly determined that the retired pilots are not entitled to have their PC3 benefits computed based on the \$160,000 IRC § 415(b) limit under EGTRRA. The Fourth Amendment, which provided the IRC § 415(b) limit increase to the retired pilots, was adopted on June 27, 2003, which was less than five years before DOPT. Thus, PBGC correctly determined that the EGTRRA increases for the retired pilots are not in PC3 because the Pilots Plan was not amended to provide them with the increases until after DOPT-5.<sup>85</sup>

Furthermore, under the Fourth Amendment, the retired pilots could not receive payments based on the increased EGTRRA limit of \$160,000 until July 1, 2002, which was less than five years before DOPT. PBGC regulations provide that the benefit in PC3 is limited to “the lowest annuity benefit *payable* under the plan provisions *at any time* during the 5-year period ending on the termination date.”<sup>86</sup> For the retired pilots, the plan provision that provides the lowest annuity benefit payable during the five-year period before DOPT is the benefit provision in effect between September 2, 2001 and June 30, 2002 (i.e., the provision that capped benefit payments based on the pre-EGTRRA IRC § 415(b) limits).

PBGC made one decision concerning PC3 benefits that is favorable to the retired pilots. Applying PBGC's automatic benefit increase provision, the 2007 Legal Memorandum concludes: “[a]lthough the EGTRRA increase is not in PC-3 for [the retired pilots], the Plan's pre-EGTRRA annual cost-of-living adjustments to IRC § 415(b) (for the fifth and four years prior to DOPT) do belong in PC-3.” PBGC further found that the pre-EGTRRA IRC § 415(b)

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<sup>82</sup> 29 C.F.R. § 4044.13(b)(6). Because the Fourth Amendment's adoption date (June 27, 2003) occurred after the effective date of its increase of the IRC § 415(b) limit for the retired pilots (July 1, 2002), the Fourth Amendment was “in effect” on June 27, 2003 for PC3 purposes.

<sup>83</sup> 29 C.F.R. § 4044.13(a).

<sup>84</sup> 29 C.F.R. § 4044.13(b)(3) (emphasis added).

<sup>85</sup> As the 2007 Legal Memorandum states, the retired pilots “needed the Fourth Amendment to have the EGTRRA increase apply to them and the Fourth Amendment was not adopted until June 27, 2003, which is less than five years before DOPT.”

<sup>86</sup> 29 C.F.R. § 4044.13(b)(3) (emphasis added).

limit would have increased to \$145,000 as of January 1, 2003, if EGTRRA had not been enacted. Thus, PBGC computed PC3 benefit amounts for the retired pilots based upon the \$145,000 limit, rather than the \$140,000 limit that was in effect at DOPT-5. The Appeal did not disagree with PBGC's conclusion that the pre-EGTRRA IRC § 415(b) limits would have increased to \$145,000 effective January 1, 2003.

The Appeals Board accepted PBGC's use of the pre-EGTRRA \$145,000 limit in calculating PC3 benefits for the retired pilots. The \$145,000 limit is more favorable to the retired pilots than the \$140,000 limit that would have been in effect at DOPT-5 in the absence of a 2003 COLA increase.

#### **4. PBGC properly excluded from PC3 the 2004, 2005, and 2006 COLA increases to the IRC § 415(b) limits**

The Appeal claims that PBGC incorrectly excluded from PC3 the benefit increases that result from the 2004, 2005, and 2006 COLAs to the IRC § 415(b) limits. AB at 17. The Appeal asserts that, for the same reasons outlined under Issue #1, the IRC § 415(b) COLAs are not "automatic increases in the benefit formula" and therefore must be included in PC3. *Id.*

The Appeals Board rejected your "automatic increases" arguments with respect to the IRC § 415(b) limit COLAs for the same reasons stated under Issue #1. As is the case with the IRC § 401(a)(17) limit COLAs, the Plan provisions that incorporated the IRC § 415(b) limit COLAs into the Plan should not be treated differently from other types of plan provisions for purposes of PC3.

The Appeals Board further decided that the 2004, 2005, and 2006 COLAs to the IRC § 415(b) limits cannot be included in a pilot's PC3 benefit because the "lowest" benefit under the plan provisions in effect in the 5-year period before DOPT is the benefit without the three COLAs. The Appeals Board made essentially the same ruling in the US Airways Decision,<sup>87</sup> which the District Court affirmed in *Davis*.<sup>88</sup> The Appeals Board rejected the Appeal's Issue #2 claim regarding the IRC § 415(b) limit COLAs for the reasons stated in the US Airways Decision and in *Davis*.

Finally, the Board decided that the 2004, 2005, and 2006 COLAs to the IRC § 415(b) limits cannot be included in a pilot's PC3 benefit under PBGC's automatic benefit increase provision in 29 C.F.R. § 4044.13(b)(5). One of the requirements in 29 C.F.R. § 4044.13(b)(5) for including an automatic benefit increase in PC3 is that the increase is "scheduled" to go into effect during the fourth and fifth years preceding [plan] termination. In the case of the 2004, 2005 and 2006 COLAs, the increases were not scheduled to go into effect – and did not actually go into effect – until (respectively) the third, second, and first year before the Pilots Plan's DOPT.

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<sup>87</sup> US Airways Decision at 19-22 (redacted copy at Enclosure 3).

<sup>88</sup> *Davis*, 864 F.Supp.2d at 157-158.

In conclusion, the Appeals Board decided that the Appeal's Issue #2 contentions do not provide a basis for changing PBGC's benefit determinations for the appellants.

**Issue 3: Whether PBGC correctly concluded that ERISA does not provide for actuarial increases to PC3 benefits for pilots who were eligible to retire three years before Plan termination, but had later benefit start dates because they remained employed by Delta. AB at 18-24.**

ERISA § 4044(a)(3) states that the benefit amount in PC3 is:

- for a participant in pay status at DOPT-3, the benefit "payable as an annuity . . . as of the beginning of the 3-year period ending on the termination date of the plan."<sup>89</sup>
- for a participant who could have but did not retire at DOPT-3, the benefit "payable as an annuity . . . if his benefits had commenced (in the normal form of annuity under the plan) as of the beginning of such [3-year] period . . . ."<sup>90</sup>

PBGC's longstanding position, based on ERISA's PC3 definition and PBGC regulation 29 C.F.R. § 4044.13, is that the PC3 annuity amount is the same for a participant who actually retired three years before plan termination and for an otherwise similarly-situated participant who decided to delay retirement. PBGC accordingly does not pay an actuarially-increased PC3 benefit to a participant who retires after DOPT-3.

### *The Appeal.*

You contend that PBGC improperly calculated benefits for those Delta pilots who were eligible for PC3 benefits but were not in pay status on DOPT-3. AB at 18-24.

Specifically, you claim that PBGC made the following two mistakes in calculating PC3 benefits for Delta pilots who were not retired on DOPT-3: (1) PBGC failed to make the "actuarially equivalent adjustment required by ERISA" to reflect that those pilots did not actually receive those pension payments until after DOPT; and (2) PBGC's decision to impose "an arbitrary three-year lookback" on a participant's age and length of service "unfairly penalizes these participants by treating them as though they chose to retire early, even though they did not." AB at 18.

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<sup>89</sup> ERISA § 4044(a)(3)(A).

<sup>90</sup> ERISA § 4044(a)(3)(B).

**Our Conclusions.**

For the reasons discussed below, the Appeals Board concluded that PBGC properly applied the rules in ERISA and PBGC regulations in calculating PC3 benefit amounts for Pilots Plan participants who were not in pay status at DOPT-3.

**Explanation of Board's Decision on Issue #3.**

Issue #3, which concerns how PC3 benefit amounts should be calculated for pilots who were not retired on DOPT-3, is identical to an issue that was decided by the Appeals Board in the US Airways Decision and the 2009 Decision. In those decisions, the Board provided a detailed explanation as to why the claim must be denied. The Board's decisions were affirmed by the U.S. District Court in *Davis*.

As explained below, the Appeals Board decided that its prior decisions on this identical issue must be applied to your Appeal.

**1. ERISA and PBGC regulations do not provide for PC3 benefit amounts to be actuarially increased for participants who are not retired at DOPT-3**

The Appeal contends that PBGC must calculate PC3 benefits "by applying principles of actuarial equivalence," which you view as "a fundamental principle of ERISA law." AB at 21. You claim that, for this reason, PBGC "must actuarially adjust the benefits of those pilots who, despite having their benefits calculated as if they had retired at DOPT-3, did not actually receive benefits at that time." *Id.*

The Appeals Board disagreed with your interpretation of ERISA's PC3 provisions. In the US Airways Decision, the Board analyzed the applicable provisions in ERISA and PBGC regulations; the Appeals Board explained its reasoning as to why the PC3 annuity amount is the same for a participant who actually retired three years before plan termination and for an otherwise similarly-situated participant who decided to delay retirement. The Board further concluded that ERISA's PC3 provision does not provide, or in any way indicate, that PC3 benefit amounts are to be actuarially increased if a participant worked or for other reasons delayed retirement after DOPT-3.

The Appeal makes an additional argument in Issue #3 that the Board did not previously address. The Appeal asserts that ERISA's PC3 definition refers to the benefit that would have "commenced" at the start of the 3-year period before DOPT because, without this language, the identification of participants "who fell within this category would have been unclear in situations where the retirement date and commencement date differed." AB at 23. You also contend that, without the "commencement date language," it would have been "more difficult to determine whether and how an actuarial adjustment should be calculated." *Id.*

The Appeals Board disagreed with your interpretation of ERISA's PC3 provision. For a participant who has not retired as of DOPT-3, but could have retired, ERISA § 4044(a)(3)(B) defines the PC3 "benefit" as "annuity" that "would have been in pay status" if the benefit "had commenced" as of the beginning of the three-year period before the termination date. Thus, ERISA § 4044(a)(3)(B) not only identifies individuals who are entitled to PC3 benefits, but it also defines the PC3 benefit amount as the annuity that would have been payable if the participant's benefit "had commenced" at DOPT-3.

**2. PBGC's "3-year lookback" in computing PC3 benefits does not constitute an improper "penalty" upon participants who did not choose to retire at DOPT-3**

The Appeal asserts that PBGC imposes an "arbitrary three-year lookback on a participant's age and length of service" when it computes PC3 benefits for participants who did not retire at DOPT-3. AB at 18. In advancing this position, you assert: (1) the Pilots Plan is designed to reward those pilots who choose to work longer, with early retirees "suffering" reductions in their pension benefits; (2) for this reason, the Pilots Plan provides a "full benefit" when a pilot retires at age 60 with 25 years of service; and (3) the impact of the Pilots Plan's terms is that the "greater the deviation from the minimum age and length of service on one's actual retirement date, the greater the penalty under the Plan." AB at 21-22. You contend that PBGC "has improperly utilized these penalties" by calculating the PC3 benefit using the participant's age and length of service at DOPT-3, which results in "unwarranted reductions in pension benefits upon participants who did not actually retire early." AB at 22.

The Appeals Board rejected essentially the same argument in the US Airways Decision.<sup>91</sup> In that decision, we held that ERISA requires PBGC to apply the pension plan's provisions when it determines the PC3 amount. In a pension plan where there are benefit reductions for participants who actually retire early, ERISA and PBGC regulations provide that the same early retirement reductions must be applied in determining PC3 benefit amounts for participants who could have retired early but chose not to do so.<sup>92</sup> Accordingly, the Board rejected your claim that PBGC improperly applied early retirement reductions when it determined PC3 benefits for Plan participants not yet retired at DOPT-3.

**3. There is no "internal inconsistency" with respect to how PBGC values and pays PC3 benefit amounts**

The Appeal asserts that there is an "internal inconsistency" because PBGC's method for valuing PC3 benefits does not correspond to the way that PBGC pays PC3 benefits. AB at 23. You state that, when PBGC values the liabilities in PC3, it assumes that "all PC3 participants actually received benefits starting on the date three years prior to Plan termination." *Id.* You further claim that, in paying PC3 benefits, PBGC "used a different method, refusing to provide

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<sup>91</sup> US Airways Decision at 17-18.

<sup>92</sup> ERISA § 4044(a)(3)(B); 29 C.F.R. § 4044.13(b)(2)(ii).

retirement-eligible participants with the pension they would have received if they had retired and had their benefits commence as of that date.” AB at 24.

The same claim was made in the US Airways Pilots Plan Appeal. In the 2009 Decision, the Board provided a detailed explanation of PBGC’s procedures for valuing the liabilities in PC3. The Board concluded in the 2009 Decision that, for the US Airways Pilots Plan, there was no inconsistency between how PBGC valued PC3 benefits and the PC3 benefit amounts that PBGC pays.<sup>93</sup> The District Court upheld this Appeals Board ruling in the *Davis* decision.

The Appeals Board found that PBGC applied the same procedures for calculating and valuing PC3 benefits for the Pilots Plan and for the US Airways Pilots Plan. Accordingly, the Appeals Board concluded that, for the reasons stated in the US Airways Decision and in the District Court’s decision in *Davis*, there is no “internal inconsistency” between PBGC’s method for valuing PC3 benefits and the way that PBGC pays PC3 benefits.

For the reasons stated above, as well as in the US Airways Decision, the 2009 Decision, and the District Court’s decision in *Davis*, the Appeals Board rejected the Appeal’s Issue #3 contentions.

## **B. PBGC’S ALLOCATION OF ASSETS AND RECOVERIES**

**Issue 4: In allocating the Plan’s assets and PBGC’s recoveries to benefit liabilities, whether PBGC disregarded \$1 billion or more in funds that allegedly “left the Plan just before PBGC assumed its role as statutory trustee.” AB at 24-26 and 29-30.**

ALPA represented Delta’s active pilots in Delta’s bankruptcy proceedings. Issue #4 relates to the funds that ALPA received from Delta on behalf of ALPA-represented pilots (the “ALPA Payments”). The ALPA Payments were made pursuant to a collective bargaining agreement amendment approved by the Bankruptcy Court judge. ALPA Payments are: (1) a \$650 million note payable from the reorganized Delta that was conditioned on the Pilots Plan’s termination; and (2) a \$2.1 billion “allowed” general unsecured claim in Delta’s bankruptcy.<sup>94</sup>

### **The Appeal.**

The Appeal asserts that, through the ALPA Payments, pilots who were active when the Plan terminated “received \$1 billion in retirement funds before anyone else was able to get their share of plan assets.” AB at 24. The Appeal contends that PBGC has a fiduciary obligation to pursue recovery of the ALPA Payments and to reallocate them “pursuant to the scheme Congress

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<sup>93</sup> 2009 Decision at 4.

<sup>94</sup> The effective date of the collective bargaining amendment is June 1, 2006. It is the Appeals Board’s understanding that distributions based on the \$650 million note and the \$2.1 billion unsecured claim: (1) were generally made to pilots who were on Delta’s System Seniority List on June 1, 2006, and (2) were not made to retired Delta pilots who were not on the June 1, 2006 seniority list.

established.” AB at 24-26. The Appeal alternatively requests that PBGC provide relief by “acknowledging that the sums received by the then-active PC4 pilots as part of the Plan termination were in fact pension benefits, and adjusting all other calculations accordingly.” AB at 26.<sup>95</sup>

### **Our Conclusions.**

The Bankruptcy Court’s order concerning the ALPA Payments is final; PBGC did not recover these funds in Delta’s bankruptcy or afterwards. The Appeals Board does not have the authority to review your claims that PBGC should pursue, or should have pursued, recovery of the ALPA Payments.

The ALPA Payments were not made from Plan assets and, thus, they were never funds that “[left] the Plan just before PBGC assumed its role as statutory trustee.” AB at 24. Furthermore, for the reasons stated below, PBGC is not required to take the ALPA Payments into account in allocating the Plan’s assets and PBGC’s recoveries. Accordingly, your request for relief under Issue #4 is denied.

### **Explanation of Board’s Decision on Issue #4.**

#### **A. Background**

On April 14, 2006, Delta and ALPA entered into Letter of Agreement #51 (“LOA #51”), titled “Bankruptcy Restructuring Agreement.”<sup>96</sup> LOA #51, which was subject to Bankruptcy Court approval, contained several significant changes affecting the pay, terms of employment, and benefits of pilots. One important provision of LOA #51 was that ALPA would not oppose the termination of the Pilots Plan, the Bridge Plan, and the SAP.<sup>97</sup>

Issue #4 centers upon two provisions in the “Bankruptcy Protection Covenant” (Attachment 28-1) that was part of LOA #51.<sup>98</sup> These two provisions state in relevant part:

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<sup>95</sup> In the Appeal Brief, your claims regarding the ALPA Payments are presented as both Issue #4 and as a part of Issue #5. See AB 24-26, 29-30. Although the facts you present and the relief you seek appear to be the same for the two claims, Issue #4 states that PBGC “erred when it allocated the remaining plan assets” and Issue #5 states that PBGC “erred when it allocated the recovered funds.” AB at 24, 29. In this decision, we combined the two parts of the Appeal that addressed the ALPA Payments into a single Issue #4.

<sup>96</sup> You provided a copy of LOA #51 in Exhibit 9 to the Appeal Brief. LOA #51 proposed changes to the then-existing collective bargaining agreement between Delta and ALPA (the PWA signed on September 21, 2001).

<sup>97</sup> Appeal Exhibit 9, LOA #51 § 26 and Attachment 28-1 at ¶ 6.

<sup>98</sup> Appeal Exhibit 9, LOA #51 Attachment 28-1 at ¶¶ 4-5 and Exhibit A.

ALPA Claim. Upon the effective date of the Bankruptcy Restructuring Agreement, ALPA will have an allowed general non-priority unsecured claim under section 502 of the Bankruptcy Code in the Bankruptcy Cases in the amount of \$2.1 billion . . . in respect of the concessions made by ALPA and savings to the Company resulting from achievement of consensual Modifications to the PWA. . . .

ALPA Notes. In the event the Delta Pilots Retirement Plan is terminated, the Company [Delta] will provide ALPA, on behalf of the Delta pilot group, with the [\$650 million in senior unsecured] notes as required by Exhibit A to this Bankruptcy Protection Covenant (the "ALPA Notes").<sup>99</sup>

On May 9, 2006, Delta filed a motion pursuant to section 363 of the Bankruptcy Code ("Section 363 Motion") in the U.S. Bankruptcy Court for the Southern District of New York (the "Bankruptcy Court").<sup>100</sup> Delta sought authorization "to enter into certain modifications to the PWA, as embodied in Letter of Agreement between Delta and ALPA . . . ."

PBGC opposed the Section 363 motion.<sup>101</sup> In particular, PBGC contended that the "ALPA Claims" and "ALPA Notes" provisions, if approved by the Bankruptcy Court, would violate Title IV of ERISA. The Bankruptcy Court, after holding a hearing on PBGC's objections, entered an order dated June 2, 2006 (the "Section 363 Order"). The Section 363 Order denied PBGC's objections and authorized Delta and ALPA to amend the PWA in accordance with LOA #51.<sup>102</sup>

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<sup>99</sup> Exhibit A describes the "Issuer" of the ALPA Notes as the "parent or affiliate of reorganized Delta Air Lines that issues common equity in connection with the Delta reorganization." Exhibit A describes the "Initial Holder" as follows:

A trust (which may be tax qualified or non qualified) or other entity not required to be registered under the Investment Company Act of 1940 for the benefit of Delta pilots or Delta pilot retirement accounts (to the extent such account is able to hold the Notes consistent with ERISA and the Internal Revenue Code), with the structure of such trust or entity to be determined by the parties, but which in no event can be a defined benefit plan (qualified or non qualified).

<sup>100</sup> *Debtors' Motion Pursuant to Section 363 of the Bankruptcy Code for Authority to Enter into Amendments to Pilot Working Agreement with Air Line Pilots Association, Int'l* (Appeal Exhibit 11). Bankruptcy Code § 363(b), 11 U.S.C. § 363(b), provides: "The [bankruptcy] trustee, after notice and a hearing, may use, sell, or lease, other than in the ordinary course of business, property of the estate." During Delta's Chapter 11 bankruptcy proceeding, section 363(b) applied to Delta in its capacity as "debtor in possession." See 11 U.S.C. § 1107, *Rights, powers, and duties of debtor in possession*.

<sup>101</sup> See Appeal Exhibit 13.

<sup>102</sup> See Appeal Exhibit 14. The Section 363 Order states: "ORDERED that the PBGC Objection is hereby overruled by the reasons stated on the record." In Enclosure 5, we provide a copy of the transcript of the May 31, 2006 hearing that the Bankruptcy Court held on PBGC's objections to the Section 363 Motion.

The Bankruptcy Court, in granting the Section 363 Order, found: (1) the relief requested in the 363 Motion was "in the best interests of the Debtors, their estates, their creditors, and all other parties in interest;" (2) entering into

PBGC timely appealed the Section 363 Order.<sup>103</sup> PBGC subsequently entered into a comprehensive Settlement Agreement with Delta, which was approved by the Bankruptcy Court on December 20, 2006.<sup>104</sup> The Settlement Agreement addressed several matters, including the Plan's termination and the amounts PBGC would receive on the bankruptcy claims PBGC filed in its corporate capacity and on behalf of the Plan. The Settlement Agreement also provided that PBGC would withdraw its appeal of the Bankruptcy Court's Section 363 Order.<sup>105</sup>

After PBGC withdrew its appeal, the Bankruptcy Court's Section 363 Order became final. Delta and ALPA subsequently amended the PWA to reflect the agreement reached in LOA #51. On April 25, 2007, the Bankruptcy Court confirmed a Plan of Reorganization for Delta.

PBGC was not the only party in Delta's bankruptcy to initially object to the Section 363 Motion. The Delta Pilot's Pension Preservation Organization ("DP3"), which represented the interests of over 6,000 retired Delta pilots,<sup>106</sup> initially opposed Delta's motion to amend the PWA through LOA #51; DP3 later withdrew its objection.<sup>107</sup> The December 12, 2006 *Response of DP3 and Trustees in Support of Debtor's Motion for Approval of Settlement Agreement with*

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LOA #51 represented "a prudent exercise of the Debtors' business judgment;" and (3) the Debtors had articulated "good, sufficient and sound business justifications and compelling circumstances for entering into LOA #51."

<sup>103</sup> See Appeal Exhibits 14, 15.

<sup>104</sup> See Appeal Exhibits 16, 17.

<sup>105</sup> See Appeal Exhibit 18.

<sup>106</sup> While you represent individual appellants in the Appeal, the Appeals Board notes that the "DP3" currently in existence asserts that "DP3 Filed an Administrative Appeal with the PBGC on Friday, October 28, 2011," and that "DP3's legal team is being led by [redacted]" See <http://dp3.org/>.

<sup>107</sup> In a May 2006 letter to DP3 members, DP3's then-Chairman [redacted] noted the following with regard to LOA #51:

Termination of the qualified plan is only indirectly addressed in this agreement but it is very important to mention. Since the termination of the qualified pension plan appears to be inevitable—and likely imminent—DP3 believes that it is in the best interests of all retired pilots drawing benefits from the plan that the highest possible funding level be assured when or if the Plan is taken over by the PBGC.

The withdrawal of our objection to LOA 51 enhances the future security of all retirees by allowing the plan to terminate in a timely manner and not risk further significant reductions in Plan funding should the Plan again be required by ERISA to resume payment of lump sums [to active pilots]. ALPA has agreed to not oppose the termination of the qualified plan in LOA 51.

See <http://www.dp3.org/data/FinalfinalChairmanLetter.pdf>.

*PBGC*, filed in U.S. Bankruptcy Court for the Southern District of New York, states the following:<sup>108</sup>

Faced with that reality [that a liquidation of the Debtors would only impose further hardships on the retired pilots] and the belief that PBGC will involuntarily terminate the plan if the lump sum window reopens, DP3 supports the Debtors' request for the approval of the settlement with PBGC. If the Pilots Plan is to be terminated, a termination which grants a substantial claim to PBGC to increase the funds available to allocate to the retirees' qualified plan payments is preferred by DP3 and its Trustees.

For the ALPA Notes, LOA #51 provides ALPA with the authority to determine “[d]istribution mechanics, eligibility and allocation . . . among pilots or pilot accounts.”<sup>109</sup> ALPA officials developed an “ALPA Notes Allocation Model” for this purpose, which is summarized in Allocation and Distribution Committee (“ADC”) Dispatches 07-09 and 07-10.<sup>110</sup> The Executive Summary of ADC Dispatch 07-09, at page 1, states that the Notes Model “addresses retirement-related issues and other items; it is not a mirror of or a replacement for the terminated Delta Pilots Retirement Plan (DPRP) or associated plans. The Model does, however, use certain factors associated with the plans as a guide.”

For the ALPA Claim, LOA #51 provides that the Delta Master Executive Council (“MEC”) “will have the authority to determine the manner of allocation among pilots on account of the ALPA Claim, provided that: (1) the allocation is reasonable and lawful and (2) the allocation schedule or formula is delivered to the Company no later than thirty (30) days prior to the date of distribution.”<sup>111</sup> As was the case with the ALPA Notes, the Delta MEC authorized the ADC to develop a “Claim Model” to determine how the ALPA Claim amounts would be allocated to

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<sup>108</sup> See <http://www.dp3.org/data/Response%20in%20Support%20of%20PBGC%20Settlement.pdf>. DP3's December 12, 2006 Bankruptcy Court filing further stated that DP3 and others “have acknowledged the value of fair and reasonable settlements which will expedite the reorganization of the company and have worked to present such settlements to the Court. This settlement is one more demonstration of that effort.”

<sup>109</sup> Appeal Exhibit 9, LOA #51 Attachment 28-1 at ¶ 5 and Exhibit A. Exhibit A provides that ALPA's decisions with respect to the ALPA Notes are subject to approval by Delta “to be exercised only as required to comply with law or distributions.” Exhibit A also states: “The allocation adopted by ALPA must be capable of being calculated and tracked by computer.” LOA #51 Attachment 28-1 at ¶ 5 and Exhibit A.

<sup>110</sup> The ALPA Notes Allocation Model was adopted by the ADC, which is a committee appointed by the Delta Master Executive Council (“MEC”) for purposes of determining how funds under the ALPA Notes and ALPA Claims were to be allocated to the accounts of individual pilots. The Delta MEC is ALPA's coordinating counsel for Delta pilots. You provided ADC Dispatches 07-09 and 07-10 in your September 21, 2012 letter to the Appeals Board (the “Sept. 2012 Letter”) as Exhibits C and D.

<sup>111</sup> Appeal Exhibit 9, LOA #51 Attachment 28-1 at ¶ 4.

individual pilots. After the Claim Model was adopted, individual pilots were provided with the opportunity to participate in a Claim sale program.<sup>112</sup>

## **B. Discussion**

Several of your contentions and requests regarding Issue #4 relate to PBGC decisions involving litigation and settlement of claims, including the following:

- PBGC, as trustee, could have sought recovery of the ALPA Payments, which you characterize as “improperly-directed Plan assets.” AB at 24-25.
- The ALPA Payments “could otherwise have gone to fund the Plan” and, if PBGC had pursued its appeal, “it likely would have had those additional resources available to it as recoveries.” AB at 26.
- PBGC, as trustee, has “an obligation to take all actions to place Appellants where they would have been monetarily had PBGC complied with ERISA.” AB at 26.
- PBGC should provide Appellants with monetary relief “by recovering the lost funds and reallocating them pursuant to the scheme Congress established.” AB at 26.

The above contentions and requests are beyond the scope of what the Appeals Board is authorized to review. PBGC’s “Rules for Administrative Review of Agency Decisions” authorize the Appeals Board to review certain initial determinations made by PBGC, including PBGC’s determinations of benefits payable to individual participants.<sup>113</sup> That regulation, however, does not provide for the Appeals Board to review PBGC’s discretionary decisions concerning: (1) the initiation and pursuit of potential claims through litigation; (2) the settlement of PBGC’s claims (including those in bankruptcy); or (3) actions PBGC could take to recover funds owed to PBGC or to PBGC-trusted pension plans.<sup>114</sup>

The Appeal also asserts that “Delta pilots who were entitled to priority in allocation of Plan assets – those in PC3 – were deprived of pension benefits ERISA mandates that they receive, while those whom Congress placed further to the back of the line – those outside PC3 – received \$1 billion in retirement funds before anyone else was able to get their share of Plan assets.” AB

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<sup>112</sup> Appeal Exhibit 10 contains an April 12, 2007 letter from [redacted] Chairman of Delta MEC, to Delta pilots. This letter states: (1) approximately 6,233 pilots opted to participate in the Claims sale program; (2) the average sale price, after all fees and expenses, was “60.05 cents on the dollar;” (3) “\$1.159 billion in value . . . will be distributed to those pilots who elected to participate in the Claim sale program;” and (4) the distribution of the cash proceeds will occur shortly after Delta emerges from Chapter 11 bankruptcy.

<sup>113</sup> See 29 C.F.R. §§ 4003.1, 4003.51.

<sup>114</sup> In the Appeal and in the Sept. 2012 Letter, you request a hearing to present evidence that relates to the Delta Bankruptcy proceedings and the Settlement Agreement that PBGC entered into with Delta. You also request that PBGC provide you with additional documents related to the Delta bankruptcy proceedings. Since these requests relate to matters that the Appeals Board is not authorized to review, the Board decided that a hearing and/or additional disclosure is not necessary.

at 24; *see also* AB at 29-30. You request that PBGC remedy this situation by “acknowledging that the sums received by the then-active PC4 pilots as part of the Plan termination were in fact pension benefits, and adjusting all other calculations accordingly.” AB at 26.

ERISA does not require PBGC to account for the ALPA Payments for purposes of allocating the Pilots Plan’s assets and PBGC’s recoveries to the Plan’s benefit liabilities. ERISA § 4044(a) provides that PBGC, upon plan termination, “shall allocate the assets of the plan (available to provide benefits) among the participants and beneficiaries of the plan.” ERISA § 4022(c) provides for PBGC to allocate a portion of its recoveries under ERISA § 4062 to benefit liabilities that are neither funded by plan assets nor guaranteed by PBGC. The ALPA Payments were never Plan assets, nor were they funds that PBGC recovered under Title IV of ERISA.<sup>115</sup>

The Appeals Board denied your request that PBGC treat the ALPA Payments as “pension payments” for purposes of the ERISA §§ 4044 and 4022(c) allocations for the Pilots Plan.<sup>116</sup> The ALPA Payments are not funds that were paid under pension plan provisions. Rather, the ALPA Payments are funds that were transferred directly from Delta to ALPA pursuant to a court-approved collective bargaining agreement. Furthermore, the ALPA Payments did not change the pension liabilities owed by the Pilots Plan to its participants and beneficiaries as of the Pilots Plan’s termination date.

For the reasons discussed above, the Appeals Board denied your relief for request in Issue #4.

**Issue 5: Whether PBGC: (A) correctly valued the funds it recovered from Delta after the Plan’s termination; and (B) correctly applied IRC limits when it allocated the ERISA § 4022(c) amount to benefits in Priority Category 5 (“PC5”). AB at 27-31.**

Issue #5 of the Appeal concerns how PBGC valued and allocated the funds it recovered from Delta. This issue contains three separate claims, one of which the Appeals Board already addressed. As explained under Issue #4, the Board denied your claim (AB at 29-30) that PBGC’s allocation of recoveries to benefit liabilities should have taken into account the ALPA Payments of over \$1 billion. In addition to the ALPA Payments claim, Issue #5 raises two additional claims regarding:

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<sup>115</sup> PBGC prepared a memorandum documenting the results of its Plan Asset Audit, which is Appeal Exhibit 34. Appeal Exhibit 34 does not list the ALPA Payments as Pilots Plan assets, nor does it suggest in any way that the ALPA Payments should be considered Plan assets.

<sup>116</sup> Although the Appeal refers generically to “pension benefits,” the benefits PBGC pays pursuant to ERISA §§ 4044 and 4022(c) allocations are for the future benefit obligations the terminated pension plan owes to its participants and beneficiaries as of the plan’s DOPT. The mere fact that a participant received a payment from a source outside of a PBGC-trusted plan does not establish that a pension liability under the terminated plan has been reduced or extinguished.

- A. Whether PBGC correctly valued the funds it recovered from Delta after the Plan's termination. AB at 27-29.
- B. Whether PBGC correctly applied IRC limits when it allocated the ERISA § 4022(c) amount to benefits in PC5. AB at 30-31.

We have identified these two claims as Issues #5.A. and #5.B., and they are addressed separately below.

**A. Whether PBGC correctly valued the funds it recovered from Delta after the Plan's termination. AB at 27-29.**

As discussed in Issue #4, PBGC negotiated a settlement with Delta that was approved by the Bankruptcy Court. PBGC determined that the total value of its recoveries under the settlement was \$1,279,506,423 as of May 3, 2007 (approximately 8 months after DOPT).

ERISA § 4022(c) requires PBGC to pay certain participants and beneficiaries "unfunded nonguaranteed benefits" based on PBGC's recoveries on its claims for "Unfunded Benefit Liabilities" ("UBL").<sup>117</sup> For purposes of its ERISA § 4022(c) calculations, PBGC used a UBL recovery value of \$988,741,430.

**The Appeal.**

The Appeal contends that PBGC made an error of "simple arithmetic" when it allocated the funds it recovered from Delta and related entities after Plan termination. AB at 27. The Appeal states that, for purposes of calculating the ERISA § 4022(c) amount, PBGC should have used the "total value" of PBGC's recovery as of the May 3, 2007 Valuation Date, which is \$1,279,506,423. AB at 28. The Appeal further claims that "[b]y valuing its recovery at \$290 million less than the amount actually recovered from Delta," the ERISA § 4022(c) amount "has been unreasonably reduced in violation of ERISA." AB at 28-29.

The Appeal requests that PBGC "either recalculate the recovery ratio and 4022(c) amount by using the actual PBGC recovery in this case (\$1,279,506,423), or provide a statutory justification for its refusal to do so." AB at 29.

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<sup>117</sup> ERISA § 4062(b) provides that a plan sponsor and members of its controlled group incur liability for the pension plan's UBL upon plan termination. UBL is defined in ERISA § 4001(a)(18).

**Our Conclusions.**

PBGC applied ERISA's requirements and PBGC policy when it determined the value of PBGC's recoveries. The UBL recovery value that PBGC determined (\$988,741,430) is less than the recovery value referenced in the Appeal (\$1,279,506,423) because:

- To reflect interest, PBGC discounted the value of PBGC's recovery as of May 3, 2007 (\$1,279,506,423) by \$50,501,683, resulting in a DOPT (September 2, 2006) recovery value of \$1,229,004,740; and
- PBGC allocated the DOPT recovery value (\$1,229,004,740) to two separate claims: (1) PBGC's claim for UBL; and (2) PBGC's claim on behalf of the Plan for Due and Unpaid Employer Contributions ("DUEC"). PBGC valued the UBL portion of the recovery as \$988,741,430 and the DUEC portion of the recovery as \$240,263,310; the combined recovery value of the two claims thus is \$1,229,004,740.<sup>118</sup>

As required by ERISA § 4022(c), PBGC allocated a large portion of the UBL recovery – \$681,259,882 out of the total UBL recovery of \$988,741,430 – to pay otherwise unfunded nonguaranteed benefits. The Appeals Board found no error in PBGC's ERISA § 4022(c) calculation and denied your request for relief under Issue #5.A.

**Explanation of Board's Decision on Issue #5.A.**

**1. ERISA § 4062 liabilities**

ERISA § 4062 establishes the employer's liability upon the termination of an underfunded single-employer pension plan. Upon the Pilots Plan's termination, Delta and its controlled group incurred the following liabilities under ERISA:

- **DUEC** are the liabilities under ERISA § 4062(c) for the accumulated "minimum funding contributions" (including interest) that a pension plan sponsor and its controlled group are required by law to contribute to the pension plan, less the amounts actually contributed. The DUEC liability is owed to a pension plan's ERISA § 4042 trustee upon the plan's termination.<sup>119</sup>
- **UBL** are the liabilities under ERISA § 4062(b) that a plan sponsor and its controlled group owe to PBGC as of DOPT for the Pilots Plan's underfunding. ERISA defines UBL, as of any date, as "the excess (if any) of—

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<sup>118</sup> PBGC used the DUEC recovery, which is treated as a Plan asset, to increase the funded PC3 benefit amounts that it pays to Plan participants based on ERISA § 4044.

<sup>119</sup> PBGC is the Pilots Plan's ERISA § 4042 trustee.

- (A) the value of the benefit liabilities under the plan (determined as of such date on the basis of assumptions prescribed by PBGC for purposes of § 4044), over
- (B) the current value (as of such date) of the assets of the plan.”<sup>120</sup>

## 2. PBGC’s total recovery from Delta has a DOPT value of \$1,229,004,740

Pursuant to PBGC’s Settlement Agreement with Delta, PBGC received recoveries for DUEC and UBL on several dates, each of which occurred after DOPT. PBGC documented its actual and expected recoveries in its *Recovery Valuation Transmittal Form*, which was approved by PBGC officials on May 5, 2009 (“Transmittal Form”), and in the *Recovery Valuation and Allocation* memorandum from PBGC’s Felece Gelb Steele to PBGC’s Andrea Schneider (“Valuation Memorandum”). You included these two documents in Appeal Exhibit 19.

Consistent with ERISA, PBGC regulations,<sup>121</sup> PBGC policy, and the documents you included in Appeal Exhibit 19, PBGC must discount recoveries to reflect their DOPT value because:

- ERISA defines both the DUEC and the UBL in terms of their value at DOPT;<sup>122</sup>
- The DUEC, which is treated as a plan asset, is valued as of DOPT for purposes of the ERISA § 4044 allocation;<sup>123</sup> and
- PBGC’s UBL recoveries are valued at DOPT for purposes of determining the ERISA § 4022(c) amounts PBGC pays to a plan’s participants and beneficiaries.<sup>124</sup>

PBGC Policy 8.2-1 details how PBGC values its recoveries.<sup>125</sup> Under this policy, PBGC first discounts the recoveries it receives to reflect their values on the “Valuation Date,” based on

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<sup>120</sup> ERISA § 4001(a)(18).

<sup>121</sup> See 29 C.F.R. § 4062.7 (calculation of interest for purposes of ERISA § 4062 liability).

<sup>122</sup> ERISA § 4062(b)(1), (c).

<sup>123</sup> See ERISA § 4044(c).

<sup>124</sup> ERISA § 4022(c)(3)(C).

<sup>125</sup> Enclosure 6 is a copy of PBGC Policy 8.2-1, *Valuation and Allocation of Recoveries*, 5<sup>th</sup> Edition (issued on July 31, 2008) (“PBGC Policy 8.2-1”). A revised PBGC Policy 8.2-1 was issued on October 10, 2012. Because PBGC completed the Plan’s valuation and allocation of recoveries in 2009, three years prior to issuance of the revised PBGC Policy 8.2-1, the 5<sup>th</sup> Edition of PBGC Policy 8.2-1 is the correct edition for PBGC to use when valuing and allocating recoveries. Therefore, references in this decision to PBGC Policy 8.2-1 relate to the July 2008 edition.

the "Appendix B" interest rate in effect on the Valuation Date.<sup>126</sup> PBGC then discounts the recoveries further to reflect their values on DOPT, based on the "Appendix B" interest rate in effect on DOPT. PBGC determined the Valuation Date for the recovery valuation to be May 3, 2007, the date when PBGC received over \$1 billion worth of Delta stock, and shortly before PBGC received a cash payment of \$225 million from Delta.

Because the Pilots Plan's Valuation Date was May 3, 2007, PBGC used the May 2007 Appendix B rate of 5.2% to discount the values of recoveries PBGC received from Delta to their values as of May 3, 2007. The table below shows how PBGC's recoveries, as documented in the Valuation Memorandum, were discounted to total a recovery value of \$1,279,506,423 as of May 3, 2007.

Recovery Date	Recovery Amount	Years after May 3, 2007 Valuation Date <sup>127</sup>	Recovery Discounted to May 3, 2007 Valuation Date <sup>128</sup>
May 3, 2007	\$1,025,328,164	0.000000	\$1,025,328,164
July 6, 2007	\$225,000,000	0.175342	\$223,008,915
February 18, 2009	\$18,907,580	1.800000	\$17,258,682
December 31, 2009	\$15,923,420	2.665753	\$13,910,662
<b>Total Discounted Recovery as of the May 3, 2007 Valuation Date</b>			<b>\$1,279,506,423</b>

Because DOPT is September 2, 2006, PBGC used the September 2006 Appendix B interest rate of 6.2% to discount the recoveries as of the Valuation Date to DOPT. Using compound interest and the assumption of 30 days per calendar month (360 days per year), the discount factor is 0.96053034  $[1/(1.062)^{(8/12 + 1/360)}]$ .<sup>129</sup> Thus, the total recovery amount as of the Plan's termination date is \$1,229,004,740  $[\$1,279,506,423 \times 0.96053034]$ .

<sup>126</sup> The "Valuation Date" is defined as the earlier of: (a) the date when all significant uncertainties as to the value of the recoveries are removed; or (b) the last day of the 16th full calendar month following the date of trusteeship of the plan.

The Appendix B interest rate is the interest rate, defined in 29 C.F.R. § 4044.52, that PBGC regulations require for valuing a terminated plan's benefit liabilities as of its DOPT. See also 29 C.F.R. § 4044.75 Appendix B to Part 4044, "Interest Rates Used to Value Benefits." Note that PBGC Policy 8.2-1.A incorrectly refers to the "29 C.F.R. section 4004 Appendix B" rate. The correct citation is the "29 C.F.R. § 4044 Appendix B" rate. There is no section 4004 in Title 29 of the Code of Federal Regulations.

<sup>127</sup> Years are calculated counting actual days (including February 29, 2008), assuming 365 days in each year. The figures in this column are shown rounded to the sixth decimal, although unrounded values were actually used.

<sup>128</sup> "Recovery Discounted to Valuation Date" equals the "Recovery Amount" multiplied by the discount from the Recovery Date to the Valuation Date (the "Discount"). The Discount equals  $1 / [(1 + 0.052) ^ n]$ , where n equals the number of years after the Valuation Date.

<sup>129</sup> While the "Years after May 3, 2007 Valuation Date" used an assumption that one year equaled 365 days, PBGC used an assumption of 30 days per calendar month (360 days per year) to discount the recovery as of the May 3,

### **3. PBGC split the \$1,229,004,740 recovery between DUEC and UBL**

As stated above, the DOPT value of PBGC's total recoveries from Delta is \$1,229,004,740. This amount reflects PBGC's combined recovery on its DUEC and UBL claims in Delta's bankruptcy. PBGC Policy 8.2-1 specifies PBGC's methodology for allocating its recoveries between DUEC and UBL. PBGC, in accordance with Policy 8.2-1, calculated the Pilots Plan's DUEC recovery as \$240,263,310 and PBGC's UBL recovery as \$988,741,430.<sup>130</sup>

The Appeal made no claim that PBGC misapplied PBGC Policy 8.2-1, and the Board did not find errors in PBGC's calculations of its recoveries from Delta.

### **4. The \$240,263,310 DUEC recovery increased the Pilots Plan's assets**

Amounts that PBGC recovers for DUEC are treated as pension plan assets (i.e., receivables) because they represent funds the plan sponsor and its controlled group owed to the pension plan as of the plan's termination date. PBGC valued the Pilots Plan's assets as \$1,984,977,782 as of DOPT, which includes the \$240,263,310 DUEC recovery. If PBGC had not received a DUEC Recovery on behalf of the Plan, the value of the Plan's assets would have been \$1,744,714,472 (\$1,984,977,782 - \$240,263,310) as of DOPT.

As explained in the Introduction to this decision, the six-tier asset allocation structure in ERISA § 4044 determines how a pension plan's assets are distributed among various benefit categories. PBGC determined that, as of DOPT, the Pilots Plan had no benefit liabilities in the first two priority categories (PC1 and PC2) and had benefit liabilities of \$2,133,502,073 in PC3. Thus, the impact of the \$240,263,310 that PBGC allocated to DUEC recovery is as follows:

- With the DUEC recovery, the Pilots Plan's assets funded 93.03847% of its benefit liabilities in PC3. This percentage is calculated as follows:  $\$1,984,977,782$  (assets)  $\div$   $\$2,133,502,073$  (PC3 benefit liabilities) = 93.03847% (PC3 funding percentage).
- Without the DUEC recovery, PC3 benefits would have been 81.77702% funded. This percentage is calculated as follows:  $\$1,744,714,472$  (assets without DUEC recovery)  $\div$   $\$2,133,502,073$  (PC3 benefit liabilities) = 81.77702% (PC3 funding percentage).

Accordingly, the \$240,263,310 that PBGC allocated to DUEC recovery significantly increased the funded PC3 benefits that PBGC pays to PC3-eligible participants and beneficiaries pursuant to ERISA § 4044, which includes the appellants.

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2007 Valuation Date back to DOPT. Both methods PBGC used to calculate interest are valid, commonly used assumptions.

<sup>130</sup> See Appeal Exhibit 19.

**5. PBGC allocated a large portion of the \$988,741,430 UBL recovery to ERISA § 4022(c) benefits**

ERISA § 4022(c) establishes a mechanism by which PBGC shares a portion of its UBL recoveries with participants. For pension plans like the Pilots Plan, in which the outstanding amount of unfunded nonguaranteed benefit liabilities (“UNGBs”) exceeds \$20 million, the section 4022(c) amount is based on PBGC’s actual UBL recovery against the plan sponsor.<sup>131</sup> Thus, ERISA § 4022(c) provides that PBGC is to use the Pilots Plan’s UBL recovery value (\$988,741,430) to calculate the Pilots Plan’s ERISA § 4022(c) amount, which is \$681,259,882 as explained below.

The first step in determining the ERISA § 4022(c) amount is to calculate the “recovery ratio.”<sup>132</sup> The recovery ratio represents the percentage of the plan’s otherwise unfunded benefits that become funded due to PBGC’s UBL recovery. For the Pilots Plan, the recovery ratio equals the DOPT value of the UBL recovery (\$988,741,430) divided by the DOPT value of the Plan’s UBL (\$2,567,680,000), which is 38.51%.<sup>133</sup>

The second (and last) step in determining the ERISA § 4022(c) amount is to multiply the DOPT value of the Pilots Plan’s UNGBs – which is \$1,769,046,686<sup>134</sup> – by the recovery ratio of 38.51%. Thus, the Pilots Plan’s ERISA § 4022(c) amount is \$681,259,882, as is shown by the following calculation:

$$\$1,769,046,686 \text{ (UNGBs)} \times 38.51\% \text{ (recovery ratio)} = \$681,259,882 \text{ (with slight increase due to rounding)}$$

As the above explanation shows, PBGC allocated a large portion of the UBL recovery – \$681,259,882 out of the total UBL recovery of \$988,741,430 – to pay otherwise unfunded nonguaranteed benefits.<sup>135</sup> The Appeals Board found no error in PBGC’s ERISA § 4022(c) calculation. Accordingly, the Board denied your Issue #5.A. claim that PBGC made an

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<sup>131</sup> ERISA § 4022(c)(2)(C). UNGBs are benefit amounts that PBGC does not pay – in the absence of recoveries – because they are not funded by the plan’s assets and are not covered by PBGC’s guarantee.

<sup>132</sup> For a plan with over \$20 million in UNGBs, ERISA § 4022(c)(3) defines the recovery ratio as “the ratio of – (i) the value of the recoveries of [PBGC] under section 4062, 4063, or 4064 in connection with such plan, to (ii) the amount of unfunded benefit liabilities under such plan as of the termination date.”

<sup>133</sup> The amounts PBGC used in its ERISA § 4022(c) calculation are documented in the Actuarial Case Memo at 1, 30-31. See Appeal Exhibit 5. As is shown in the Actuarial Case Memo, the Pilots Plan’s UBL of \$2,567,680,000 is the difference between the DOPT value of the Plan’s benefit liabilities (\$4,552,657,782) and the DOPT value of the Plan’s assets (\$1,984,977,782).

<sup>134</sup> The \$1,769,046,686 amount for UNGBs is shown in the Actuarial Case Memo at 1, 31.

<sup>135</sup> The remaining portion of the UBL recovery, \$307,481,548, provides partial compensation to PBGC for its payment of the Pilots Plan’s unfunded guaranteed benefits (“UGBs”).

“arithmetic error” in determining the benefits that PBGC pays to Pilots Plan participants under ERISA § 4022(c).

**B. Whether PBGC correctly applied IRC limits when it allocated the ERISA § 4022(c) amount to benefits in Priority Category 5 (“PC5”).** AB at 30-31.

Issue #5.B. concerns how PBGC allocated the ERISA § 4022(c) amount to benefits in PC5. PBGC does not guarantee benefits in PC5. PBGC further cannot pay all benefit amounts in PC5 because the Pilots Plan’s assets and the ERISA § 4022(c) amount did not fully fund them.

ERISA § 4044(b)(4) instructs how PBGC is to allocate the ERISA § 4022(c) amount in PC5. ERISA § 4044(b)(4) establishes two priority subcategories within PC5. The higher priority subcategory within PC5 applies to the benefits “under the plan as in effect at the beginning of the 5-year period ending on the date of plan termination.” The lower priority subcategory covers benefits under plan provisions that went into effect on later dates, i.e., after DOPT-5. ERISA § 4044(b)(4) provides that benefits in the lower priority PC5 subcategory cannot be funded by plan assets and/or by PBGC’s recoveries unless all benefits in the higher priority PC5 subcategory are funded.

PBGC concluded that the benefit increases that occurred after DOPT-5 due to the IRC limit increases must be included in the lower priority PC5 subcategory. PBGC further found that PBGC cannot pay the IRC limit increases or any of the other benefits assigned to the lower priority PC5 subcategory because the Plan’s ERISA § 4022(c) amount was exhausted after funding 51.95696% of the benefits in the higher priority PC5 subcategory.

**The Appeal.**

The Appeal contends that PBGC’s ERISA § 4022(c) allocation was improper because it did not accord priority within PC5 to IRC § 401(a)(17) and IRC § 415(b) limit increases. The Appeal states: “[A]ssuming *arguendo* that the IRC provisions could fairly limit PC3 benefits, those same limits should have been removed when distributing funds in PC5.” AB at 30 (emphasis in original). The Appeal requests that PBGC reallocate PBGC’s recoveries and make any necessary adjustments to individual benefit determinations.<sup>136</sup> AB at 31.

**Our Conclusions.**

The Appeals Board decided that PBGC properly allocated the ERISA § 4022(c) amount for the Pilots Plan to the PC5 subcategories. Accordingly, the Board denied the Issue #5.B. claim in the Appeal.

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<sup>136</sup> Although the Appeal states at AB 31 that “PBGC should reallocate Plan assets” in PC5, the Appeal appears to be referring to PBGC’s allocation of recoveries, since the Plan’s assets were insufficient to fund any benefit liabilities in PC5.

**Explanation of Board's Decision on Issue #5.B.**

**1. ERISA's requirements for allocating the ERISA § 4022(c) amount to PC5 benefits**

PC5 benefits are nonforfeitable benefits that (1) are not guaranteed (i.e., are not in PC4) due to ERISA's guarantee limits, and (2) do not meet the requirements for inclusion in one of the higher priority categories, such as PC3. PBGC determined that the ERISA § 4022(c) amount funded approximately 34.4% of the Pilots Plan's benefit liabilities in PC5.<sup>137</sup>

As stated above, ERISA § 4044(b)(4) instructs how PBGC must allocate plan assets and recoveries when they are sufficient to fund some, but not all, benefits in PC5. Unlike the other priority categories, ERISA does not provide for a pro rata allocation to individuals who have benefits in PC5. Instead, the statute separates PC5 benefits into two subcategories of benefits, known as PC5(a) and PC5(b).<sup>138</sup>

Subcategory PC5(a) covers PC5 amounts "under the plan as in effect at the beginning of the 5-year period ending on the date of plan termination."<sup>139</sup> ERISA provides that Subcategory PC5(a) benefits must be fully funded before any funds may be allocated to benefits in Subcategory PC5(b).<sup>140</sup>

If Subcategory PC5(a) is fully funded, then the allocation of funds to Subcategory PC5(b) benefits is "determined on the basis of the plan as amended by the most recent plan amendment effective during such 5-year period [before DOPT]."<sup>141</sup> Thereafter, priority for the allocation of funds to Subcategory PC5(b) benefits is determined "on the basis of the plan as amended by the next succeeding plan amendment effective during such period."<sup>142</sup>

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<sup>137</sup> The Actuarial Case Memo at pages 1 and 31, details how PBGC allocated the Pilots Plan's ERISA § 4022(c) amount. The Memo shows that PBGC first allocated \$111,795,637 of the Pilots Plan's ERISA § 4022(c) amount to UNGBs in PC3. PBGC then allocated the remaining portion of the ERISA § 4022(c) amount, \$569,464,245, to benefit liabilities in PC5. PBGC determined that the total PC5 liability of the Pilots Plan is \$1,654,258,317.

<sup>138</sup> See also 29 C.F.R. § 4022.10(e) (PBGC regulation concerning allocation of assets within priority categories, including the PC5 subcategories).

<sup>139</sup> ERISA § 4044(b)(4)(A).

<sup>140</sup> ERISA § 4044(b)(4)(B).

<sup>141</sup> *Id.*

<sup>142</sup> *Id.*

## 2. PBGC's allocation of the ERISA § 4022(c) amount to benefits in PC5

PBGC determined that the Pilots Plan's Subcategory PC5(a) liability – which is entitled to priority under the PC5 allocation – totaled \$1,096,030,648.<sup>143</sup> A large portion of that liability is for Plan benefits above the MGB for participants who are not PC3-eligible.<sup>144</sup> Additionally, many PC3-eligible participants who retired after DOPT-3 have benefits in Subcategory PC5(a).<sup>145</sup>

PBGC concluded that a plan provision is in effect for Subcategory PC5(a) purposes on the date that it is operative. Thus, PBGC did not assign a benefit increase to Subcategory PC5(a) if the applicable Pilots Plan provision was not “in effect” (i.e., was not operative) until after DOPT-5. PBGC applied this rule to all increases under the Pilots Plan's provisions, including the provisions that: (1) capped compensation based on the IRC § 401(a)(17) limit; and (2) limited benefit payments in accordance with the IRC § 415(b) limit. PBGC assigned the benefit increases that occurred after DOPT-5 to the lower priority PC5 subcategory (i.e., Subcategory PC5(b)).<sup>146</sup> PBGC has treated PC5 benefits in a similar manner in other plans.

Because the Plan's ERISA § 4022(c) amount funded only 51.95696% of the PC5 liabilities in Subcategory PC5(a), PBGC determined that there were no remaining funds to allocate to Subcategory PC5(b).

## 3. The effective date of benefit increases under the PC5 subcategories

The Appeal disagrees with PBGC's conclusion that increases to Plan benefits due to increases in the IRC limits in 2002, 2004, 2005, and 2006 must be assigned to the lower priority PC5(b) subcategory. The Appeal asserts that, if the benefit increases resulting from the IRC limit increases are not in PC3, they must be included in the higher priority PC5(a) Subcategory. AB at 31. In advancing this position, the Appeal essentially contends that “effective date” may

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<sup>143</sup> See Actuarial Case Memo at 31. In the Actuarial Case Memo, “PC5a” refers to benefits in Subcategory PC5(a) and “PC5b-PC5l” refers to benefits in Subcategory PC5(b). See also Actuarial Case Memo at 30, which lists the Pilots Plan's benefit liabilities in all priority categories, including the subcategories within PC5.

<sup>144</sup> For such participants, the Subcategory PC5(a) amount is the Plan benefit amount calculated under plan provisions in effect at DOPT-5 less the PC4 amount.

<sup>145</sup> Such participants have benefits in Subcategory PC5(a) generally because they accrued additional benefits after DOPT-3 and/or because the early retirement factor applicable on their retirement date is greater than the early retirement factor applicable at DOPT-3. For such participants, the Subcategory PC5(a) amount is the benefit calculated under Plan provisions in effect at DOPT-5, but not greater than the DOPT Plan benefit, less the amounts in PC3 and in PC4 (if any).

<sup>146</sup> The IRC limit increases that increased Plan benefits after DOPT-5 for some appellants are: (1) the EGTRRA increase to the IRC § 401(a)(17) limit that went into effect on July 1, 2002 (approximately 4 years and 2 months before DOPT); (2) the EGTRRA increase to the IRC § 415(b) limit that, under the Plan's provisions, went into effect for retired pilots on July 1, 2002; (3) the IRC § 401(a)(17) COLAs that went into effect in 2004 and 2005; and (4) the IRC § 415(b) COLAs that went into effect in 2004, 2005, and 2006.

have a different meaning for purposes of assigning benefits to the subcategories within PC5 than for purposes of determining PC3 amounts. AB at 30-31.

Accordingly, to resolve Issue #5.B. of the Appeal, the Appeals Board needed to determine when a plan provision or a plan amendment is “in effect” for purposes of assigning benefits to the two subcategories within PC5.

Although this issue has not previously been raised in an appeal, the Appeals Board has decided similar issues for purposes of determining PC3 benefit amounts pursuant to ERISA § 4044(a)(3) and for purposes of the phase-in limitation of PBGC’s guarantee pursuant to ERISA § 4022(b)(1) and (7). With regard to both the PC3 benefit and phase-in limit, the Appeals Board consistently has decided that a benefit increase under a plan provision or amendment is “in effect” on the date the increase becomes operative, unless the provision or amendment has a later adoption date or stated effective date.

As explained below, the Appeals Board decided that the same rules governing when a plan provision or amendment is “in effect” for purposes of determining the PC3 benefit and applying the phase-in limit should be applied in assigning benefits to the PC5 subcategories. Accordingly, PBGC correctly allocated the Pilots Plan’s ERISA § 4022(c) amount to benefits in subcategory PC5(a).

The Appeals Board based its decision on this issue on ERISA’s statutory structure regarding the benefits that PBGC pays. ERISA § 4044(b)(4), which establishes the PC5 subcategories, is similar to ERISA’s PC3 and phase-in limit provisions because the provisions each contain a 5-year look-back period based upon when a plan provision or amendment is “effective” or “in effect.” The similar language in these three statutory provisions is evident from the following:

- ERISA § 4044(a)(3) states that PC3 benefits are “based on the provisions of the plan (as in effect during the 5-year period ending on [DOPT]) under which such benefit would be the least;”
- ERISA § 4022(b)(1), which relates to PC4 benefits, states that the phase-in limit applies to: (i) “benefits provided by a plan which has been in effect for less than 60 months at the time the plan terminates;” and (ii) “any increase in the amount of benefits under a plan resulting from a plan amendment which was made, or became effective, whichever is later, within 60 months before the date on which the plan terminates . . .,”<sup>147</sup> and

<sup>147</sup> Additionally, ERISA § 4022(b)(7) states that PBGC’s guarantee is phased in:

only to the extent of the greater of—

(A) 20 percent of the amount which, but for the fact that the plan or amendment has not been in effect for 60 months or more, would be guaranteed under this section, or

(B) \$20 per month,

- ERISA § 4044(b)(4)(A) provides that benefits in subcategory PC5(a) are determined “under the plan as in effect at the beginning of the 5-year period ending on the date of plan termination.”<sup>148</sup>

As discussed under Issues #1 and #2, PBGC interprets ERISA’s PC3 provision as providing that a benefit increase cannot be “in effect” for purposes of PC3 before the date when the increase becomes operative.<sup>149</sup> As previously noted, a United States District Court has upheld PBGC’s interpretation on this point.<sup>150</sup>

Similarly, for the phase-in limit, ERISA § 4022 provides that, a plan provision or amendment is not “in effect” until it “first becomes effective” (i.e., becomes operative). This is evident from ERISA § 4022(b)(7), which states:<sup>151</sup>

In determining how many years a plan or amendment has been in effect for purposes of this paragraph, the first 12 months beginning with the date on which the plan or amendment is made or first becomes effective (whichever is later) constitutes one year, and each consecutive period of 12 months thereafter constitutes an additional year.

There is nothing in other Title IV provisions or in ERISA’s legislative history to indicate that the words “effective” and “in effect” were intended to have a special meaning for purposes of PC5, as compared to PC3 and PC4. Accordingly, the natural inference is that the terms should be construed similarly.

The Appeals Board further concluded that the PC3 provisions, the phase-in limit applicable to PC4, and the PC5 provisions should be construed similarly because, under ERISA § 4044, any benefit amount not assigned to a higher priority category will be assigned to a lower one. It

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multiplied by the number of years (but not more than 5) the plan or amendment, as the case may be, has been in effect.

<sup>148</sup> ERISA § 4044(b)(4)(B) similarly provides that benefits in Subcategory PC5(b) are determined “on the basis of the plan as amended by the most recent plan amendment effective during such 5-year period” and “on the basis of the plan as amended by the next succeeding plan amendment effective during such period.”

<sup>149</sup> See ERISA § 4044(a)(3); see also PBGC’s PC3 regulation at 29 C.F.R. § 4044.13(b)(3).

<sup>150</sup> *Davis*, 864 F.Supp.2d at 157.

<sup>151</sup> See also PBGC regulation 29 C.F.R. § 4022.24(e), § 4022.25(b). PBGC regulation 29 C.F.R. § 4022.24(e) states that “a benefit increase is deemed to be in effect commencing on the later of its adoption date or its effective date.” 29 C.F.R. § 4022.25(b) provides that PBGC’s guarantee under the “phase-in formula” is based on “the number of years the benefit increase has been in effect, not to exceed five.” Thus, PBGC’s regulations provide that a benefit increase is in effect for phase-in purposes when it becomes operative.

would be illogical to apply a different “effective date” rule for purposes of the PC5 subcategories than the rule for determining PC3 benefits and the guaranteed PC4 amounts.<sup>152</sup>

The Appeal contends that the Board must apply the Appeal’s interpretation of PC5 even if the Board rejects the Appeal’s similar interpretation of PC3 (*see* discussions under Issues # 1 and #2). The Appeal attempts to distinguish ERISA’s PC5 provisions concerning PC5 subcategories from ERISA’s PC3 provision on the basis that the PC3 language, unlike the PC5 provision, refers to “benefits” in “pay status” and “benefits” that are “the least.” AB at 30-31.

The Appeals Board found such distinctions made in the Appeal to be unpersuasive because the PC3 language you cite does not define the “effective date” of plan provisions. The Board further found that the PC3 and the PC5 subcategories provisions are worded differently for the following reasons:

- The PC3 provision’s references to “pay status” relate to the eligibility requirements for that priority category. To be in PC3, a benefit must either be in pay status at DOPT-3 or would have been in pay status at DOPT-3 if the participant had retired.

For PC5 and its subcategories, however, there are no requirements that the participant be in pay status or eligible to enter into pay status as of a particular date.<sup>153</sup>

- Reference to “such benefit that would be the least” in the PC3 provision relates to benefit amounts that are covered by the priority category. PC3 does not cover all nonforfeitable benefits provided by the pension plan. Instead, ERISA requires that the plan administrator (or PBGC) assign to PC3 the benefit amount that is the lowest under all plan provisions that are in effect in the five years before plan termination.<sup>154</sup>

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<sup>152</sup> For example, a benefit increase that went into effect two years before DOPT will be phased-in for PC4 purposes at the greater of 40% or \$40 per month, even if the applicable plan provision was adopted before DOPT-5. The remaining nonforfeitable amount that is not in PC4 (i.e., the remaining 60% of the increase, or the portion of the increase above \$40) is assigned to PC5.

<sup>153</sup> PC5 includes both nonforfeitable benefits in pay status and nonforfeitable benefits that first become payable on future dates (which are commonly referred to as “deferred vested benefits”).

<sup>154</sup> As previously discussed, the benefit in PC3 is the amount payable at DOPT-3 or that would be payable at DOPT-3 if the participant had retired.

We observe that the most recent plan provision in the 5-year period before DOPT does not always provide the largest benefit amount for purposes of PC3. For example, a plan could adopt an amendment 4 years before DOPT (“DOPT-4”) that immediately freezes benefit accruals. For such a plan, a participant who retired after the freeze could have a larger PC3 amount under the DOPT-5 provisions than under the DOPT-4 provisions. The PC3 benefit in this example is the smaller amount computed under the DOPT-4 provisions.

PC5, by contrast, covers the participant's remaining nonforfeitable benefit after amounts are assigned to higher priority categories. Under ERISA's PC5 allocation provisions, there is no need to determine the benefit that is the "least."<sup>155</sup>

In summary, the Appeals Board found no compelling reason to distinguish between the effective dates of plan provisions in PC3 and in the PC5(a) subcategories, as you propose. Rather, it is logical to apply the same rule regarding when a plan provision or amendment is "in effect" to the PC3 provision, phase-in limit, and PC5 provisions. This, in fact, has been PBGC's practice for every PBGC-trusted plan, including the Pilots Plan. Thus, Subcategory PC5(a) does not include Plan benefit increases that occurred within five years of DOPT due to increases in the IRC limits.

#### **4. Additional contentions in Issue #5.B.**

Finally, the Appeal contends that the increased benefits that appellants received as a result of IRC limit increases are entitled to priority within PC5 because: (1) the IRC limits "should have placed no limitation on Plan assets available to participants whose benefits were entitled to PC3 status;" (2) there is "no rational basis" to apply a 5-year look-back period to the IRC limits on benefit payments; and (3) the IRC limits are not "plan provisions." AB at 30-31. The above assertions essentially reiterate the claims, previously made in Issues #1 and #2 of the Appeal, that increases to IRC limits should be treated differently than other types of benefit increases under pension plan provisions. The Board denied these Issue #5.B. contentions for the reasons stated above under Issue #1 and Issue #2.

Accordingly, for the above reasons, the Appeals Board denied the Appeal's claims for relief under Issue #5.B.

### **C. PBGC'S PAYMENT OF GUARANTEED BENEFITS**

**Issue 6: Whether PBGC correctly interpreted and applied the ERISA provisions applicable to guaranteed benefit amounts. AB at 31-36.**

The Maximum Guaranteed Benefit ("MGB") limit in ERISA § 4022(b)(3) places a cap upon "the amount of monthly benefits . . . provided by a plan, which are guaranteed under this section with respect to a participant."<sup>156</sup> Throughout its history, PBGC has viewed its guarantee

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<sup>155</sup> For PC5, the plan administrator (or PBGC) computes the participant's nonforfeitable benefit under all plan provisions in effect in the five years before plan termination in order to assign the appropriate amounts to the PC5 subcategories. The plan's assets and PBGC's recoveries are then allocated to the PC5 subcategories according to their priority (e.g., Subcategory PC5(a) must be fully funded before Subcategory PC5(b) receives an allocation).

A participant's total benefit in the PC5 subcategories, when combined with the benefit in higher priority categories, cannot exceed the participant's total nonforfeitable benefit under the pension plan. The rules in PBGC's PC3 regulation (*see* 29 C.F.R. § 4044.10(e)) prevent such an outcome.

<sup>156</sup> ERISA § 4022(b)(3) defines the amount of the MGB's cap, stating that the monthly guaranteed amount:

obligation under ERISA as ensuring that each participant will receive, subject to the other ERISA guarantee limits, the plan's nonforfeitable benefit up to the MGB's statutory cap regardless of the Plan's funding. Where a plan's assets will pay the statutorily-guaranteed amount, PBGC incurs no liability. If the plan's assets are insufficient to provide statutorily-guaranteed benefits, as frequently is the case in PBGC-trusted plans, PBGC must use its own funds to provide such benefits to participants and beneficiaries.

Participants and beneficiaries are sometimes entitled to more than their guaranteed benefit amount, based on the allocation of the plan's assets under ERISA § 4044(a). In such cases, PBGC pays the larger of (1) the benefit funded by the allocation of plan assets, or (2) the PBGC-guaranteed benefit amount.<sup>157</sup>

### **The Appeal.**

The Appeal contends that appellants are entitled to additional benefits because PBGC incorrectly applied the MGB limit. AB at 31-36. Essentially, the Appeal asserts that the MGB is a limit on the "insurance" that PBGC is required to pay to each participant from PBGC's own funds, rather than a minimum benefit amount guaranteed to each participant. AB 31-32. The Appeal requests that PBGC pay appellants "their non-forfeitable benefits not covered by the remaining plan assets, subject to the statutory maximum." AB at 36.

### **Our Conclusions.**

The Appeals Board decided that PBGC properly applied the rules in ERISA and PBGC's regulations to ensure that all eligible Pilots Plan participants and beneficiaries receive, at a minimum, their nonforfeitable benefits up to the statutorily-guaranteed limits.

### **Explanation of Board's Decision on Issue #6.**

Issue #6 is identical to a claim in the US Airways Pilots Plan Appeal that was rejected by the Appeals Board in the 2009 Decision. The issue raised in that appeal, as here, involves the relationship between PBGC's obligation to pay guaranteed benefits and its obligation (as trustee) to pay benefits based on the allocation of a terminated plan's assets. The US Airways Pilots Plan

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shall not have an actuarial value which exceeds the actuarial value of a monthly benefit in the form of a life annuity commencing at age 65 equal to . . . \$750 multiplied by a fraction, the numerator of which is the contribution and benefit base (determined under § 230 of the Social Security Act) in effect at the time the plan terminates and the denominator of which is the contribution and benefit base in effect in calendar year 1974.

<sup>157</sup> In addition, PBGC pays any ERISA § 4022(c) amount that a participant or beneficiary is entitled to receive. See discussion under Issue #5.

Appeal similarly asserted that PBGC “is required to pay from its insurance funds all non-forfeitable benefits (up to a statutory maximum) once Plan assets are exhausted.”<sup>158</sup>

As the Appeals Board explained in its June 2009 decision, the above-stated reading of PBGC’s guaranteed benefit obligation represents a major departure from the way PBGC has consistently interpreted ERISA’s statutory language and from over 30 years of PBGC practice in making benefit determinations. Further, ERISA’s basic structure concerning PBGC’s guarantee and the allocation of plan assets to benefits has not changed for single-employer plans since ERISA was enacted in 1974.

In the 2009 Decision, the Appeals Board rejected the guaranteed benefits interpretation in the US Airways Pilots Plan Appeal. The Board, after an extensive analysis of applicable statutory and regulatory provisions, concluded that “PBGC as guarantor is not responsible for assuring payment of plan benefit amounts that exceed [ERISA’s] statutorily-prescribed limits, regardless of whether or not part of the benefit is funded by plan assets.”<sup>159</sup> The Board’s ruling on this issue was affirmed by the District Court in *Davis*.<sup>160</sup>

The Appeals Board rejected the interpretation of PBGC’s guarantee obligation advanced in the Appeal for the reasons stated in the 2009 Decision and in *Davis*. Accordingly, the Appeals Board denied you request for relief under Issue #6.

#### **D. PBGC’s BENEFIT CALCULATIONS**

**Issue 7: Whether PBGC properly calculated benefits for participants who were eligible to have their benefits calculated under the Plan’s Minimum Benefit formula. AB at 36-38.**

The Pilots Plan contains a Final Average Earnings (“FAE”) formula that applies to all Plan participants.<sup>161</sup> The Pilots Plan also contains a Minimum Benefit formula that applies to certain participants.<sup>162</sup> For Minimum Benefit-eligible pilots, the Plan benefit is the greater of the FAE formula amount, which includes a Social Security Administration Offset (“SSA Offset”), and the Minimum Benefit formula amount, which has no SSA Offset provision.

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<sup>158</sup> 2009 Decision at 8.

<sup>159</sup> *Id.* at 14.

<sup>160</sup> See also *Davis v. PBGC*, 571 F.3d 1288, 1292-93 (D.C. Cir. Jul. 10, 2009) (discussion of PBGC’s guarantee obligation).

<sup>161</sup> Plan § 1.18 (definition of “Formula Benefit”). For Issue #7 and Issue #8, when we use the term “Plan” with respect to a particular Pilots Plan provision, we are referring (unless stated otherwise) to the provision in effect when the Pilots Plan terminated, i.e., the provision in the 1996 Restatement as modified by later Plan amendments.

<sup>162</sup> Plan § 8.02.

**The Appeal.**

The Appeal asserts, "it appears that eligible Plan participants are being denied the Minimum Benefit." AB at 37. The Appeal states that Plan § 8.02 provides that participants who meet the Minimum Benefit eligibility requirements on or after July 1, 1996 "will in no event receive an annual benefit at Normal Retirement Date less than" the amount under the Minimum Benefit formula. AB at 36-37. The Appeal further contends that PBGC applied the Minimum Benefit formula incorrectly by: (1) offsetting at least one appellant's benefit for Social Security payments;<sup>163</sup> and (2) utilizing the IRC § 401(a)(17) limit to reduce benefits. AB at 37-38. The Appeal requests that "PBGC review and correct all its final benefit determinations for those Plan participants who are eligible to receive the Minimum Benefit." AB at 37.

**Our Conclusions.**

The Appeals Board found 499 appellants who met the eligibility criteria under the Plan's Minimum Benefit provision. The Board further found that Delta and/or PBGC determined the Pilots Plan benefit for these 499 individuals as the higher of the benefit under the Minimum Benefit formula and the benefit under the FAE formula. Thus, no eligible appellants are being denied the Minimum Benefit.

The Board further found that Delta and PBGC appropriately applied the IRC § 401(a)(17) limit in calculating benefits pursuant to the Minimum Benefit formula.

Finally, the Appeals Board found that Delta and PBGC generally applied the Plan's SSA Offset provisions correctly for the 499 Minimum Benefit-eligible appellants. The Board identified six appellants, however, who have errors in their SSA Offsets. The Board's correction of these errors will slightly increase the PBGC-payable benefit for three appellants and will slightly decrease the PBGC-payable benefit for three appellants.

With the exception of the six appellants referenced above, the Appeals Board denied your Issue #7 contentions.

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<sup>163</sup> The Appeal further asserts, "Appellants believe that this practice of offsetting Minimum Benefit payments for Social Security benefits is widespread." AB at 37.

Plan § 5.03 of the Plan explicitly refers to "Social Security reduction" while the Appeal uses the term "Social Security Offset." The terms have the same meaning and are used interchangeably in this decision.

**Explanation of Board's Decision on Issue #7.**

**A. Background**

**1. The Pilots Plan's benefit formulas**

Plan § 1.18, which defines the term "Formula Benefit," sets forth how benefit amounts under the Pilots Plan are to be calculated.<sup>164</sup> As stated in Plan § 1.18, the Formula Benefit is the monthly single life annuity ("SLA") amount that is the greater of: (1) the benefit determined under the FAE formula; and (2) for Minimum Benefit-eligible participants, the benefit determined under the Minimum Benefit formula.

The Minimum Benefit formula, which is set forth in Plan § 8.02, applies to pilots who were Delta employees on February, 1 1972.<sup>165</sup>

The FAE formula and Minimum Benefit formula represent two different types of benefit calculations. The FAE formula provides a benefit that is based on the pilot's Credited Service (up to 25 years) and the pilot's Final Average Earnings (which is a 36-month average based on highest earnings).<sup>166</sup> Earnings typically increased during the course of employment with Delta; thus, pilots' earnings near the end of their careers ordinarily have a significant impact upon the size of their Pilots Plan benefits under the FAE formula.

The Pilots Plan's Minimum Benefit formula – which contains both a "fixed" and "variable" component – is a "career average pay" arrangement.<sup>167</sup> The Minimum Benefit formula is a

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<sup>164</sup> Several Plan provisions that address the benefit amounts participants and beneficiaries are entitled to receive from the Pilots Plan, including § 4.02 ("Forms of Benefit Payment") and § 5.04 ("Payment of Benefit"), refer to the "Formula Benefit."

<sup>165</sup> Specifically, Plan § 8.02 identifies Minimum Benefit-eligible participants as: "Participants in the Plan who were also Participants in the Delta Air Lines Employees' Retirement Income Plan and the Delta Air Lines Employees' Variable Annuity Retirement Income Plan as of February 1, 1972, or who were Employees of Delta Air Lines on February 1, 1972." The two pension plans named in Plan § 8.02 were prior plans sponsored by Delta that were replaced by the Pilots Plan.

Additionally, three groups of pilots are listed in the Plan document as having joined Delta later than February 1, 1972. These groups include former Northeast Airlines pilots, former Western Air Lines, Inc. pilots, and former Pan Am pilots. See Plan §§ 8.03, 2.03, and 5.03. Former Northeast Airlines pilots have their own Minimum Benefit formula provided in § 8.03 of the Plan, and a small number of appellants were former Northeast Airlines pilots whose benefits were calculated under the Northeast Minimum formula. The Minimum Benefit formula that applied to Northeast Airlines pilots was not raised in the appeal and is not discussed further in this decision.

<sup>166</sup> Plan § 1.18 defines the FAE formula amount for a SLA as "the ratio of the Employee's Credited Service to 25, with a maximum ratio of 1.0 times 60% of the Employee's Final Average Earnings, both determined as of the Employee's Retirement Date or other date of Termination of Continuous Employment."

<sup>167</sup> As provided in Plan § 8.02 and the Twelfth Amendment to the 1996 Restatement at ¶ 12, the Minimum Benefit includes the benefit amounts the pilot had accrued (if any) before February 1, 1972 under two prior pension plans

“career average pay” arrangement because a pilot accrues additional Minimum Benefit amounts each year based on a percentage of each year’s earnings. Thus, a pilot’s earnings near the end of his or her career tend to have a smaller impact upon the Minimum Benefit amount than upon the FAE formula amount.

Significantly, the variable component of the Minimum Benefit formula was frozen as of July 1, 1996, which also is the date when future accruals under the fixed component were reduced from 2% to 1% of the pilot’s earnings.<sup>168</sup> As a result of these 1996 changes, the additional benefit amounts that the pilot accrued after July 1, 1996 under the Minimum Benefit formula were relatively small. By contrast, there were no changes in the FAE formula that reduced accruals until credited service was frozen on December 31, 2004. The overall impact of the larger post-1996 accruals under the FAE formula as compared to the Minimum Benefit formula is that almost all Minimum Benefit-eligible pilots who retired in the five years before the Pilots Plan’s termination had the highest Formula Benefit under the FAE formula. The Board identified only two appellants who retired after DOPT-5 with the highest Formula Benefit under the Minimum Benefit formula.

## **2. The Delta calculation methodology**

PBGC accepted and applied the methodology that Delta used for calculating the “Formula Benefit” under the Pilots Plan. The “Delta Formula Benefit Calculation Methodology,” which is described in Appendix B, implemented the Pilots Plan’s provisions under which, for Minimum Benefit-eligible pilots, the Formula Benefit is the greater of the FAE formula amount and the Minimum Benefit formula amount.

The Appeals Board found that PBGC did not err in adopting the Delta Formula Benefit Calculation Methodology described in Appendix B.

## **3. The Appeals Board’s review of Pilots Plan records**

When PBGC became trustee of the Pilots Plan, Delta provided PBGC with electronic data and hard-copy records. PBGC relied on such data and records in reviewing and calculating Plan

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sponsored by Delta. Additionally, the pilot earned additional annual accruals starting February 1, 1972, under the fixed component of the Minimum Benefit formula, which equaled 2% of the pilot’s earnings between February 1, 1972 and June 30, 1996 and 1% of the pilot’s earnings between July 1, 1996 and the earlier of the pilot’s retirement date and July 31, 2006. Finally, under the variable component of the Minimum Benefit formula, the pilot accumulated “benefit units” from February 1, 1972 through June 30, 1996 based on his earnings; the values of the benefit units were adjusted by an investment return index. At retirement, the benefit units are converted to an annuity benefit.

The “Retirement Benefits” section of the *Pilot Benefits Handbook* dated May 1, 1997 (Enclosure 7) explains the Minimum Benefit formula.

<sup>168</sup> The 1996 changes to the Minimum Benefit are set forth in a Pilots Plan amendment dated June 12, 1996 and the 1996 Restatement § 8.02. See also Twelfth Amendment to the 1996 Restatement (freeze of all benefit accruals under the Pilots Plan effective July 31, 2006).

benefits and PBGC-payable benefits for participants and beneficiaries.<sup>169</sup> Section 19 of the Actuarial Case Memo describes the extensive checks and reviews conducted by PBGC actuaries in reviewing benefit calculations, including calculations under the Minimum Benefit formula. Data PBGC obtained typically included benefit amounts under the FAE formula and, where applicable, the Minimum Benefit formula.

For all 499 Minimum Benefit-eligible appellants, the Appeals Board reviewed the electronic data that Delta provided to PBGC. To confirm the accuracy of this electronic data, the Appeals Board reviewed hard-copy records for a sample of 160 Minimum Benefit-eligible appellants. Enclosure 8 summarizes the Board's findings for the 160 appellants whose hard-copy records the Board reviewed.

## **B. Discussion**

### **1. PBGC did not ignore the Minimum Benefit formula**

The Appeal asserts, “[d]espite the fact that every Plan participant who was employed as of February 1, 1972 is eligible for the Minimum Benefit, and thus should be receiving the benefit in any case where the benefit exceeds what the participant would have received pursuant to the Formula Benefit, it appears that eligible participants are being denied the Minimum Benefit.” AB at 37.<sup>170</sup>

The Appeal does not provide a single example to support its general allegation that PBGC “ignored” the Plan’s Minimum Benefit provision.

As stated above, the Appeals Board reviewed electronic data and hard-copy pension records for Minimum Benefit-eligible appellants. The Appeals Board found that, for all Minimum Benefit-eligible appellants, Delta and PBGC calculated the Plan’s Formula Benefit using both the Minimum Benefit formula and the FAE formula, as explained in Appendix B. The Board further found that, for these appellants, the Pilots Plan benefit amount always is based on the greater of the FAE formula amount and the Minimum Benefit formula amount.

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<sup>169</sup> See Actuarial Case Memo at 31-47.

<sup>170</sup> Furthermore, the Appeal asserts the following:

PBGC also appears to have erred when it ignored the Plan’s minimum benefit provision. We say “appears to” because the basis for the PBGC’s benefit determinations is far from clear. But to the extent the PBGC did ignore that long-standing Plan provision, doing so was [in] error.

AB at 36.

## 2. Application of the IRC § 401(a)(17) limit to Minimum Benefit calculations

The Appeal asserts that PBGC improperly applied the IRC § 401(a)(17) limit to reduce benefits under the Minimum Benefit formula. In support of your assertion, you cite an internal PBGC memorandum.<sup>171</sup> This internal PBGC memorandum incorrectly states that the Minimum Benefit formula does not take into account earnings. The Appeals Board found that the misstatement was inadvertent and had no impact on PBGC's calculation of benefits for Minimum Benefit-eligible appellants.

Plan § 8.02(B) provides that, for time periods beginning February 1, 1972, the Minimum Benefit is calculated based on the pilot's "Earnings." Furthermore, the Plan's definition of "Earnings" in § 1.12 incorporates by reference the various IRC § 401(a)(17) limit provisions that were enacted into law. Accordingly, the IRC § 401(a)(17) limits must be applied to a pilot's earnings in determining the Minimum Benefit amount.<sup>172</sup>

Based on the Pilots Plan's provisions, the Appeals Board denied your claim that PBGC improperly applied the IRC § 401(a)(17) limit to reduce benefits under the Minimum Benefit formula.

## 3. Application of the Plan's SSA Offset to Minimum Benefit-eligible individuals

Plan § 5.03 requires the application of the Plan's SSA Offset when an individual's benefit is highest under the FAE formula. If the individual's benefit is highest under the Minimum Benefit formula, no SSA Offset is applied.<sup>173</sup>

The Appeal cites Appeal Exhibit 28, the benefit determination of appellant [redacted] for the proposition that PBGC improperly applied a SSA Offset to participants whose benefit is the highest under the Minimum Benefit formula. PBGC did not apply a SSA Offset to Mr. [redacted]'s benefit, and we found no evidence that Delta applied a SSA Offset to his benefit on his 65<sup>th</sup> birthday in [redacted] 2001 or on an earlier date.<sup>174</sup>

The Appeal further states that appellants believe that PBGC's "practice of offsetting Minimum Benefit payments for Social Security benefits is widespread." AB at 37. The Appeal

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<sup>171</sup> See Appeal Exhibit 23.

<sup>172</sup> The IRC § 401(a)(17) limit was initially established through enactment of TRA '86 and was effective in 1989. The limit thus applied to all pilots with earnings in and after 1989. See detailed explanation of IRC § 401(a)(17) in Issue #1.

<sup>173</sup> Plan § 8.02(B)(v) provides that "[n]o reduction for Social Security benefits will be applied against the minimum benefit."

<sup>174</sup> Mr. [redacted] filed his own individual appeal (Appeal # [redacted]), which was decided by the Appeals Board on [redacted]. Mr. [redacted] did not claim in his appeal that PBGC (or Delta) improperly applied a SSA Offset to his benefit. The Appeals Board sent a copy of its decision on Mr. [redacted] individual appeal to Mr. [redacted] of your firm.

requests that “PBGC review and correct all its final benefit determinations for those Plan participants who are eligible to receive the Minimum Benefit.” *Id.*

In response to the Appeal’s assertions concerning the SSA Offset, the Appeals Board reviewed electronic pension data and hard-copy records, as previously stated.<sup>175</sup> The Board, based on its review, found:

- Delta’s and PBGC’s consistent practice was to apply the SSA Offset, as required by Plan § 5.03, if the participant’s total Formula Benefit was higher under the FAE formula than under the Minimum Benefit formula. If a participant’s total benefit was higher under the Minimum Benefit formula, then Delta’s and PBGC’s consistent practice was not to apply a SSA offset.
- If a pilot’s benefit required a SSA Offset, Delta consistently applied that reduction at age 65 (unless the reduction was required earlier due to early commencement of Social Security benefits or election of a survivorship form of benefit).<sup>176</sup>
- Delta performed an internal review to ensure the SSA Offset would not be applied to pilots whose Formula Benefit was highest under the Minimum Benefit formula.<sup>177</sup>
- Hard-copy pension records we reviewed often contained letters from Delta explaining when the Social Security reduction, if applicable, would take effect.<sup>178</sup>

Although Delta typically applied a SSA Offset in accordance with the Plan’s provisions (i.e., at the pilot’s age 65), PBGC discovered that Delta failed to apply a required SSA Offset for some pilots who reached age 65 in 2005 and 2006. PBGC corrected this Delta oversight when it issued benefit determinations; PBGC applied the SSA Offset to these individuals’ benefits effective October 1, 2006, which is the first PBGC benefit payment date after the Plan’s termination.

The Board’s review identified three additional appellants for whom Delta failed to apply a required Social Security reduction. PBGC did not correct Delta’s errors when it issued benefit determinations to these three individuals. This decision corrects the Delta and PBGC errors by applying a SSA Offset effective October 1, 2006, which decreases the PBGC-payable benefits of the following three appellants:

- Mr. [redacted] (Appeal # [redacted]; see Enclosure 11)
- Mr. [redacted] (Appeal # [redacted]; see Enclosure 12)

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<sup>175</sup> See Enclosure 8 (Board’s findings for 160 appellants based on review of hard-copy records).

<sup>176</sup> See further discussion under Issue #8.

<sup>177</sup> See Enclosure 9 for a Delta letter regarding the internal review.

<sup>178</sup> See Enclosure 10 for copies of such Delta letters in the files of 10 appellants.

- Mr. [redacted] (Appeal # [redacted]; see Enclosure 13)

Finally, the Board discovered that PBGC erred in applying SSA Offsets to the benefits of three appellants who should not have had SSA Offsets because their Formula Benefits are highest under the Minimum Benefit formula. These errors occurred in a small group of pilots whose benefits were impacted by Qualified Domestic Relations Orders. This decision corrects PBGC's errors by eliminating the SSA Offset, which increases the PBGC-payable benefits of the following three appellants:

- Mr. [redacted] (Appeal # [redacted]; see Enclosure 14)

- Mr. [redacted] (Appeal # [redacted]; see Enclosure 15)

- Mr. [redacted] (Appeal # [redacted]; see Enclosure 16)

New Benefit Statements, which are provided in the above-listed enclosures, state the corrected benefit amounts determined by the Appeals Board for five of the appellants. The Appeals Board has not determined the corrected benefit for Mr. [redacted] because he has an open individual appeal; his benefit (with no SSA Offset) will be corrected when the Board decides his individual appeal.

PBGC's Benefits Administration and Payment Department ("BAPD"), the office responsible for determining and paying benefits, will notify these appellants of the amounts they have been underpaid or overpaid and will make necessary corrections to their monthly benefit payments.

The Appeals Board did not identify any other Minimum Benefit-eligible appellants who had SSA Offset errors or whose benefits otherwise were incorrect. In conclusion, except for the six appellants with errors noted above, the Appeals Board denied the appeal on Issue #7.

**Issue 8: Whether PBGC applied the Social Security Administration Offset at an earlier age than the Plan's provisions authorized. AB at 38-39.**

**The Appeal.**

The Appeal objects to how PBGC determined PBGC-payable benefit amounts for appellants who are impacted by the SSA Offset under the FAE formula. While the Appeal states that "[c]onsistent with the Plan, the PBGC properly utilized this [SSA] offset procedure in calculating the initial PC3 benefit of the Plan's participants," the Appeal contends that "in calculating the *final* benefit determinations for Appellants, the PBGC has ignored the language of the Plan and 'levelize[d]' Appellants' benefits by prematurely applying a Social Security offset prior to the time authorized in the Plan." AB at 38 (emphasis in original).

According to the Appeal, "PBGC's premature offset practice penalizes those participants who have not yet reached age 65 by depriving them of benefits to which they are entitled today, to the benefit of PBGC itself." AB at 39. In footnote #10 (AB at 39), the Appeal asserts that

PBGC, "in at least one instance," failed to properly calculate the SSA Offset for "Plan participants initially hired by Pan Am or Western Air Lines."

The Appeal requests that "PBGC review and correct all its final benefit determinations for whom the PBGC has improperly applied the Social Security offset," including the determinations for the three pilots identified in Appeal Exhibit 31. AB at 39.

### **Our Conclusions.**

The Appeals Board found that PBGC determined the correct start dates for the SSA Offset to appellants' benefits, in accordance with the Plan's terms.

Pilots Plan participants with the SSA Offset often have non-level benefits because the SSA Offset does not begin immediately (e.g., the Pilots Plan benefit may start at age 60 with the reduction for the SSA Offset starting at age 65). When the PBGC-payable benefit amounts are non-level and less than the Plan benefit amounts, PBGC uses a "Percentage Method" to calculate PBGC-payable benefit amounts.<sup>179</sup> Under the Percentage method, an individual's PBGC-payable non-level benefit amount will equal a percentage (based on present values) of the individual's non-level Plan benefit amount.

If an individual's PBGC-payable benefit amount is less than the Plan benefit amount, the Percentage Method results in a smaller (and proportional) monthly SSA Offset for the PBGC-payable benefit as compared to the Plan benefit. As explained below and in Appendix C, the adjustments PBGC makes in computing SSA Offsets do not provide a financial gain to PBGC. The Appeals Board upheld PBGC's method for determining appellants' SSA Offsets as reasonable.

Finally, the Board found that PBGC and Delta calculated the proper SSA offset for Plan participants initially hired by Pan Am or Western Air Lines. Accordingly, the Board denied your Issue #8 contentions.

### **Explanation of Board's Decision on Issue #8.**

#### **A. Background**

The SSA Offset is applied only when the larger Formula Benefit is calculated using the FAE Formula; if the Minimum Benefit formula provides a larger Formula Benefit, then the participant will have no SSA Offset.<sup>180</sup>

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<sup>179</sup> The "Plan benefit" is the benefit PBGC would pay if the Pilots Plan had been fully funded. If the individual's non-level PBGC-payable amounts equal the individual's non-level Plan benefit amounts, then PBGC applies a percentage of 100% (i.e., there will be no reduction to the Plan benefit amounts).

<sup>180</sup> See Issue #7 discussion.

The SSA Offset, which is required by § 5.03 of the Plan, equals (i) 50% of the participant's Primary Social Security Benefit ("PSSB") (ii) multiplied by the ratio of the participant's Credited Service to 25 years (with a maximum ratio of 1.0).<sup>181</sup>

The Pilots Plan provides that for participants with seniority dates prior to February 9, 1982, the relevant PSSB is \$233.30.<sup>182</sup> The vast majority of appellants have a seniority date prior to February 9, 1982. Thus, for these participants, the age-65 SSA Offset cannot exceed \$116.65 (50% of \$233.30). For participants who have seniority dates after February 9, 1982, the relevant PSSB is \$647.50, and the age-65 SSA Offset for appellants cannot exceed \$323.75 (50% of \$647.50).<sup>183</sup>

The effective date of the SSA Offset depends on the benefit form. In the case of a SLA, the SSA Offset is calculated assuming a Social Security benefit start date at age 65 and is applicable on the first of the month following the participant's 65<sup>th</sup> birthday.<sup>184</sup> If the participant elects to commence Social Security benefits before age 65, the SSA Offset amount is reduced for early commencement using SSA factors and is applied at the time Social Security benefits actually commence.<sup>185</sup>

Plan § 5.03 further states the following (additional) rule for the SSA Offset:

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<sup>181</sup> Plan § 1.28 defines the term "Primary Social Security Benefit" as "[a]n amount which would be available as a monthly old age benefit, exclusive of benefits for a Spouse or other relatives or dependents . . . ." The 1996 Restatement § 5.03 and Second Amendment at ¶ 9 address how PSSB amounts are determined. Plan § 5.03 was amended twice after the 1996 Restatement, by the Second Amendment (adopted June 24, 2002 and effective September 1, 2002) and the Fourth Amendment (adopted June 27, 2003 and effective July 1, 2002).

<sup>182</sup> Specifically, the Second Amendment at ¶ 9 provides that, for pilots with a seniority date prior to February 9, 1982, the PSSB cannot "exceed the amount of such benefit reduction which a person reaching age 65 in 1973 would receive had his Earnings in each calendar year in which he worked exceeded the Social Security Taxable Wage Base for that year." Under that definition, the maximum PSSB for a pilot with a seniority date prior to February 9, 1982 is \$233.30.

<sup>183</sup> The Second Amendment at ¶ 9 provides that, for pilots with a seniority date after February 8, 1982, the PSSB cannot exceed the Social Security maximum for a person attaining age 65 in 1982, which is \$647.50. We found at least 66 appellants with a seniority date after February 9, 1982; these appellants will have a SSA Offset (if applicable) that cannot exceed \$323.75 (50% of \$647.50).

<sup>184</sup> See Plan § 5.03.

<sup>185</sup> *Id.* The Pilots Plan sometimes did not start the SSA Offset before age 65 if a pilot had not informed Delta that his or her Social Security benefit started.

If the SSA Offset begins before age 65, the SSA Offset amount is reduced using Social Security Administration factors equal to 5/9 of 1% per month for each of the 36 months Social Security benefits are received preceding age 65. See Social Security Handbook at [http://www.ssa.gov/OP\\_Home/handbook](http://www.ssa.gov/OP_Home/handbook).

Notwithstanding [other Plan provisions concerning] the timing of the Social Security offset . . . , in the case of a Participant whose annuity benefit commences before age 65 in the form of a joint and survivor annuity or in the form of a joint and 50% contingent annuity, the Actuarial Equivalent of this reduction will be applied beginning on the Participant's Annuity Starting Date.

## **B. Discussion**

### **1. Start dates for the SSA Offset**

PBGC did not change the way that Delta administered the Plan's SSA Offset provisions. For most appellants impacted by the SSA Offset, Delta and PBGC applied the SSA Offset at age 65.

In accordance with Plan provisions, Delta and PBGC also applied the SSA Offset prior to age 65 in instances where the Plan's terms provide for an earlier offset (e.g., when the participant notified Delta or PBGC that he or she had commenced Social Security benefits before age 65). The Appeals Board found Delta's and PBGC's practice concerning the SSA Offset start date to be consistent with the Pilots Plan's provisions.

In Appeal Exhibit 31, you provide benefit determinations, benefit statements, and detailed benefit statement worksheets for three individuals: [redacted], [redacted], and [redacted]. Mr. [redacted] and Mr. [redacted] are appellants in the Appeal; Mr. [redacted] is not an appellant because his appeal was not timely filed. You state that the documents you provided are examples of PBGC's application of the SSA Offset "prior to the time authorized in the Plan, i.e., prior to age 65 (and prior to the actual commencement of receiving Social Security benefits)." AB at 38.

PBGC did not prematurely apply a SSA Offset to the PBGC-payable benefits of these three individuals. The Appeals Board found:

- PBGC started the SSA Offset for Mr. [redacted] with his [redacted], 2007 PBGC benefit payment. [redacted], 2007 was the first day of the month after he reached age 65.
- Mr. [redacted] retired at age 55 and [redacted] months on [redacted], 2003. In [redacted] 2010, Mr. [redacted] notified PBGC that he had commenced his Social Security benefits. Accordingly, PBGC properly applied his SSA Offset effective [redacted], 2010 ([redacted] months before age 65), consistent with the Plan's terms.
- PBGC has not started the SSA Offset for Mr. [redacted]. PBGC will commence Mr. [redacted]'s SSA Offset on [redacted], 2014, the first day of the month after his 65th birthday, or on an earlier date if he informs PBGC that he has started his Social Security benefits.

For appellants impacted by the SSA Offset (i.e., their highest Formula Benefit is under the FAE formula), the Appeals Board did not find any instance where PBGC started the SSA Offset before the date authorized under the Pilots Plan's terms.

## 2. SSA Offset amounts computed by PBGC and the Percentage Method

For some appellants, the PBGC-payable benefit amount is the same as the Plan benefit amount. For these appellants, PBGC applies the full SSA Offset as prescribed by the Plan.

The PBGC-payable benefit amount is less than the Plan benefit for many appellants with the SSA Offset. For these individuals, PBGC uses a "Percentage Method" to calculate the monthly amounts PBGC pays. As stated above, PBGC does not change the SSA Offset start date in these calculations.

Appendix C provides a detailed explanation of PBGC's Percentage Method as it relates to the SSA Offset under the Pilots Plan.<sup>186</sup> Appendix C uses appellants [redacted] and [redacted] as examples of how PBGC applies the Percentage Method.

The Appeal claims that "PBGC has ignored the language of the Plan and 'levelize[d]' Appellants' benefits by prematurely applying a Social Security offset prior to the time authorized in the Plan." AB at 38. The Appeal also asserts that PBGC's offset practice "penalizes those participants who have not yet reached age 65 by depriving them of benefits to which they are entitled today, to the benefit of PBGC itself." AB at 39.

The Appeal inaccurately characterizes PBGC's calculation method. The adjustments PBGC makes under the Percentage Method are based on the present values of the monthly non-level benefit amounts that PBGC initially calculates based on the Plan's terms and PBGC's regulations.<sup>187</sup> The impact of the Percentage Method is that the SSA Offset amount is reduced in proportion to the reduction in the individual's Plan benefit.

The Appeals Board found that the Percentage Method does not have the detrimental effect that the Appeal suggests. PBGC's Percentage Method adjustments do not decrease the actuarial values of the monthly amounts that PBGC initially calculates under the Pilots Plan's terms. The Appeals Board further concluded that PBGC's use of the Percentage Method to determine SSA Offset amounts is consistent with Title IV of ERISA, PBGC regulations, and PBGC policy. Accordingly, PBGC did not err in applying the Percentage Method.

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<sup>186</sup> The Percentage Method also is explained in a PBGC document titled "Actuary response to [redacted]'s August 12, 2010 letter," which is Appeal Exhibit 30.

<sup>187</sup> Under the Percentage Method, PBGC initially calculates the individual's (1) monthly PC3 benefit, (2) monthly guaranteed benefit, and (3) monthly Plan benefit. PBGC then converts these monthly benefit amounts to present values for purposes of determining the PBGC-payable benefit. See explanation in Appendix C. The PBGC-payable benefit for the Pilots Plan is the greater of the funded PC3 benefit and the PBGC-guaranteed benefit, plus the ERISA § 4022(c) amount.

### 3. SSA Offset amounts for former Pan Am and Western Air Lines pilots

Footnote #10 of the Appeal states:

For Plan participants who were initially hired by Pan Am or Western Air Lines, the Social Security offset is determined by reference to a specified ratio (the product of the Participant's Social Security Benefit and the ratio of the Participant's length of service to a 25-year period). Appellants note that the PBGC has, in at least one instance, failed to properly apply this ratio, and, given the dearth of information which the PBGC supplies to Plan Participants, it is the obligation of the PBGC, as Plan's trustee, to ensure that the offset is done correctly on behalf of those Participants

AB at 39.

The Pilots Plan's formal document states that the Social Security Offset is computed using the specified ratio discussed in this footnote when the larger Formula Benefit is calculated using the FAE Formula.<sup>188</sup> The Plan's document also specifically states how this Social Security Offset ratio is determined for former Pan Am and Western Air Lines pilots.<sup>189</sup> Because the Appeal does not further identify the "one instance" of an error, the Board is unable to specifically respond to this allegation. The Board reviewed electronic data for all former Pan Am and Western Air Lines pilots. The Board found that Delta and PBGC properly calculated the applicable SSA Offset using "the ratio of the Participant's length of service to a 25-year period"<sup>190</sup> to reduce, as appropriate, the applicable SSA Offset.

For the above-stated reasons, the Appeals Board denied the contentions made in Issue #8.

### E. OTHER CLAIMS

**Issue 9: Whether PBGC should re-audit the Pilots Plan's assets.** AB at 40-41 and AB Supp. at 2-3.

#### The Appeal.

The Appeal requests that PBGC conduct another audit of the Pilots Plan's assets because the initial audit may have been flawed. The Appeal further asserts that, to the extent any

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<sup>188</sup> The 1996 Restatement § 5.03 and Second Amendment at ¶ 9.

<sup>189</sup> *Id.*

<sup>190</sup> Footnote #10 of the Appeal.

discrepancies are discovered through another audit, PBGC should “immediately recalculate Appellants’ benefit determinations.” AB at 39-40; AB Supp. at 2-3.

In requesting another audit, the Appeal refers to two Evaluation Reports issued by the Office of Inspector General for PBGC (“OIG”).<sup>191</sup> The OIG Evaluation Reports identified deficiencies in the asset audits PBGC conducted for terminated pension plans formerly administered by United Airlines and National Steel. AB at 39; AB Supp. at 2.

The Appeal further notes that PBGC engaged a third-party contractor, Integrated Management Resources Group (“IMRG”), to perform the Pilots Plan asset audit. AB at 40. IMRG also performed the asset audits for the National Steel and United Airlines pension plans that were the subjects of the OIG Evaluation Reports. The Appeal contends that PBGC should conduct another asset audit for the Pilots Plan in light of IMRG’s history of providing “substandard and obviously flawed work.” AB at 40; AB Supp. at 2-3.

### **Our Response.**

As you state in the Appeal Brief and Supplemental Appeal Brief, two Inspector General reports identified flaws in how PBGC contractor IMRG valued the assets of pension plans and in how PBGC handled oversight of that contractor. After these two OIG Evaluation Reports were issued, PBGC took steps to implement new procedures to improve the asset audit process.

Senior PBGC officials have informed the Appeals Board that PBGC has hired a public accounting firm to undertake a plan asset re-evaluation for the Pilots Plan. The Appeals Board is not involved in the asset re-evaluation process for the Pilots Plan and does not know when it will be completed. PBGC will keep Plan participants, beneficiaries, and alternate payees updated on the status of the asset re-evaluation on the [www.pbgc.gov](http://www.pbgc.gov) public website. Should PBGC-payable benefits require adjustment, PBGC will make them. The results of the Pilots Plan asset re-evaluation, when completed, will be available on request from the PBGC Disclosure Officer.

**Issue 10: Whether PBGC’s application of its appeal time limits improperly denied some individuals the right to join the Appeal.** AB at 41-45 and AB Supp. at 3.

### **The Appeal.**

The Appeal is critical of how the Appeals Board applied PBGC’s 45-day limit for filing appeals and the “good cause” exception to that limit. PBGC’s regulations require that a participant, beneficiary, or alternate payee file an appeal – or request an extension of time to file

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<sup>191</sup> These two OIG Evaluation Reports are: *PBGC’s Plan Asset Audit of National Steel Pension Plans Was Seriously Flawed* (March 30, 2011); and *PBGC Processing of Terminated United Airlines Pension Plans Was Seriously Deficient* (November 30, 2011).

an appeal – within 45 days after the date of PBGC’s initial determination.<sup>192</sup> The Appeals Board may accept an untimely appeal if the individual requesting review demonstrates “good cause” as to why a timely appeal was not filed.

The Appeal claims that the Board improperly denied appeal rights to approximately 300 of your clients on the basis of untimeliness and failure to demonstrate “good cause.” The Appeal asserts that the Board “should allow every individual who has been listed as a member of the appeal in Exhibit 1 to formally become part of this appeal.” AB at 45.

### **Our Conclusions.**

The Appeals Board applied PBGC’s “45-day filing rule” regardless of whether the appeal filing was made by an individual or by your firm on behalf of an individual. The Board also examined, and approved, a number of requests that otherwise untimely appeals be accepted for good cause. As a result, the Board docketed appeals for 1,498 of your clients (over 80% of the individuals named in the Appeal).

Because the Appeals Board correctly applied PBGC’s regulations governing the timely filing of appeals, the Board denied your request for relief on Issue #10.

### **Explanation of Board’s Decision on Issue #10.**

The Appeal makes several assertions regarding the Appeals Board’s 45-day filing rule. The Appeal states that the rule:

- is not jurisdictional, citing *Henderson v. Shinseki*, 131 S. Ct. 1197 (2011) (AB at 41);
- has been enforced in a “completely arbitrary fashion” (AB at 41);
- is “irrational and erroneous” (AB at 42);
- is “draconian” in the context of the informal nature of the appeals process (AB at 42);
- is “particularly troubling” because the Appeal “was delayed for over a year by the failure of the information officers at the agency [PBGC’s Disclosure Officer] to produce” necessary information (AB at 43); and
- has no “rational basis” given that “unrepresented participants” did not fully understand PBGC’s appeal rules when they received their determinations (AB at 43).

In short, you disagree with the PBGC 45-day filing rule and ask that the Board not apply it to your clients.

PBGC’s regulations establish the procedures governing administrative appeals, including the general requirement that an individual must appeal PBGC’s determination within 45 days of the

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<sup>192</sup> See 29 C.F.R. §§ 4003.1, 4003.4(a), and 4003.52.

determination or request an extension of time to file an appeal within the same 45-day period.<sup>193</sup> The Appeals Board applies these procedures uniformly to all participants, beneficiaries, and alternate payees in PBGC-trusted pension plans, regardless of whether the appeal filing is made by that individual or that individual's representative.

Enclosure 17 explains how the Board determined that 1,498 participants and beneficiaries represented by your firm are timely-filed appellants. This number includes: (1) 1,476 individuals who met the 45-day filing rule, either through their own appeal filing or by a filing by your firm on their behalf; and (2) 22 additional individuals whose untimely appeals were accepted by the Board under the "good cause" exception in PBGC's regulation.<sup>194</sup>

We concluded that the Appeal does not establish a compelling rationale as to why the Appeals Board should allow the exceptions you seek to the 45-day filing requirement, either for reasons of general applicability or based on the specific circumstances of your clients. The 45-day filing rule is an important part of PBGC's administrative process that is designed to permit the Agency to implement its determinations without undue delay, as explained below.

PBGC issues benefit determinations to notify participants, beneficiaries, and alternate payees in writing of the benefits they are entitled to receive from PBGC.<sup>195</sup> Under PBGC's regulation, an initial determination "will not become effective until the prescribed period of time for filing [an appeal] has elapsed."<sup>196</sup> If an appeal is filed within the 45-day period, the determination does not "become effective" until the appeal is decided.<sup>197</sup> Likewise, if the Board grants an individual an extension of time to file an appeal, the determination does not "become effective" until either the extension of time has expired with no appeal filed or, if an appeal is timely filed, the date the appeal is decided.<sup>198</sup>

For the majority of PBGC benefit determinations, no appeal or request for an extension of time to file an appeal is made in the 45-day filing period. In such cases, PBGC's formal determination becomes effective after the expiration of the 45-day time period; PBGC then implements the terms of the benefit determination, including necessary adjustments to the individual's monthly benefit. Thus, the 45-day filing period is consistent with PBGC's goals of having an efficient process for ensuring that benefits are paid to participants, beneficiaries, and

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<sup>193</sup> *Id.*

<sup>194</sup> *See* 29 C.F.R. § 4003.5.

<sup>195</sup> *See* 29 C.F.R. § 4022.21.

<sup>196</sup> 29 C.F.R. § 4003.22(a).

<sup>197</sup> *Id.*

<sup>198</sup> *See* 29 C.F.R. §§ 4003.22(a) and 4003.4.

alternate payees in the correct amounts while allowing individuals to present their claims to the Appeals Board.

The Appeals Board disagreed with your contention that the Board should waive the 45-day filing requirement "because unrepresented participants who wanted to appeal did not fully understand the PBGC's appeal rules at the time." AB at 43. PBGC explains the 45-day filing rule in every formal determination. Every benefit determination issued to Pilots Plan participants and beneficiaries contains the following language:

This is PBGC's formal determination of your benefit. You have the right to appeal this determination if you provide a specific reason why the determination is wrong. Your appeal must be in writing and filed within 45 days of the date of this letter. If you simply have a question about how your benefit was calculated, you should call us for an explanation, instead of filing an appeal. But please note that the time you have to file an appeal will not be extended unless you specifically request an extension within the 45-day period. The enclosed pamphlet, *Your Right to Appeal*, explains more about filing an appeal.

A copy of *Your Right to Appeal*, which is enclosed with every benefit determination, is at Enclosure 18. This pamphlet provides detailed information on how to file an appeal or request additional time to file an appeal. To assist participants and beneficiaries, the Appeals Board provides optional forms (PBGC Forms 723 and 724) that may be used for such filings. The Board accepts filings by mail, fax, and email. The Board also provides answers to frequently asked questions about the appeals process on PBGC's website at [www.pbgc.gov/prac/appeals-board/appeals-decisions-faq.html](http://www.pbgc.gov/prac/appeals-board/appeals-decisions-faq.html).

The Appeals Board recognized that the Board's application of the 45-day filing rule means that some of your clients will not have their claims decided by the Appeals Board. In deciding the Appeal, however, the Board did not find any information or decide any Appeal issue that suggests your non-appellant clients may be receiving incorrect benefit amounts.<sup>199</sup>

In summary, the Appeals Board followed PBGC's regulations governing the timely filing of appeals. The Appeals Board denied your request for relief on Issue #10.

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<sup>199</sup> If in deciding an appeal the Appeals Board finds information indicating that similarly-situated non-appellants may be receiving incorrect benefit amounts, the Board notifies BAPD of our findings. BAPD then reviews Plan records and decides whether individual benefits should be changed for these non-appellants. With respect to the Appeal, the Board found errors in the benefits of six appellants caused by incorrect SSA Offsets. In researching these SSA Offset errors, we found five additional non-appellant participants (none of whom are your clients) with incorrect SSA Offsets. We notified BAPD of the SSA Offset errors for these five participants, and BAPD is sending them corrected benefit determinations. Finally, PBGC policy provides that any Plan participant, beneficiary, or alternate payee may always submit specific evidence to BAPD indicating an error in his or her benefit; BAPD will review that evidence and respond to the concern raised.

**Issue 11: Whether individual appellants may supplement the Appeal and raise additional individual issues. AB at 45-46.**

**The Appeal.**

The Appeal expressly reserves the right of each appellant to supplement the Appeal and to raise additional issues through individual appeals. The Appeal states that some appellants are waiting for additional information from PBGC pursuant to Freedom of Information Act (“FOIA”) requests. The Appeal reserves the right of such individuals to supplement the Appeal with individual issues “when complete information becomes available.” AB at 45.

**Our Response.**

The Appeals Board informed your firm orally and in writing soon after the Appeal was filed that we would permit your firm to supplement the Appeal and would provide timely-filed appellants with the opportunity to raise their own individual appeal issues.<sup>200</sup> The Board’s action is consistent with the long-standing Appeals Board practice of permitting any appellant to supplement his or her appeal until the date the Board issues its decision. The Board also extended appeal-filing deadlines so that Pilots Plan participants, beneficiaries, and alternate payees could receive information from PBGC’s Disclosure Officer before filing their individual appeals.

Your firm supplemented the Appeal with the Supplemental Appeal Brief. Likewise, several appellants raised their own individual issues after the Appeal was filed. The Board docketed all timely-filed individual appeals.<sup>201</sup> When the Appeals Board decides an individual appeal, the Board will continue the practice of providing your firm with a copy of the decision.

**Issue 12: Whether PBGC failed to meet its fiduciary responsibility to the appellants. AB at 45-48 and AB Supp. at 3.**

**The Appeal.**

The Appeal contends that PBGC failed to act with prudence, diligence, and solely in the interest of Plan participants and beneficiaries. AB at 46. Specifically, you assert that PBGC either denied or failed to respond in a timely manner to appellants’ requests for information necessary to evaluate the accuracy and propriety of PBGC’s benefit determinations. *Id.* The Appeal also contends that when PBGC did provide information to appellants, there was a divergence in the quality and substance of the information. AB at 47.

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<sup>200</sup> See Board’s letter to your firm dated December 21, 2011 at Enclosure 19.

<sup>201</sup> See Enclosure 20 (list of 13 open individual appeals and two open extension requests).

You further assert that the Benefit Determination Letters (“BDLs”) issued to all participants, beneficiaries, and alternate payees lack the information necessary for actuaries to verify calculations relating to final benefit amounts. AB at 46-47. You disagree with PBGC’s practice of providing Benefit Statement Worksheets (“BSWs”) only upon request, rather than as part of BDLs. AB at 48. You note that the BSWs contain more details about PBGC’s benefit calculations than the Benefit Statements PBGC provides as enclosures to its BDLs. *Id.*

You assert that many PBGC calculations rely on determinations made by the former Plan administrator. AB at 47. You note that, in May 2010, you requested all documents in PBGC’s possession that underlie appellants’ benefit determinations. *Id.* You state that, because PBGC was unable to honor this request, appellants were forced to narrow the request to a sampling of documents generated by the former Plan administrator. *Id.*

Finally, the Appeal contends that the Appeals Board does not act as a fair and impartial tribunal because it appears that PBGC lawyers who will represent PBGC in any litigation “are playing an integral role in resolving the questions presented to the Appeals Board.” AB at 48. You request that the Board “disclose any ex parte contacts that it has had concerning this appeal with the lawyers who will eventually defend the agency in future litigation.” AB at 48.

#### **Our Response.**

The Appeals Board responded to the issues raised above in letters sent to you on December 21, 2011 and May 1, 2012.<sup>202</sup> Among other things, the Appeals Board’s letters explained the processes by which PBGC issues benefit determinations and provides information to appellants.

BAPD determines benefits and provides BDLs to every participant, beneficiary, and alternate payee. If BAPD determines a benefit amount that is different than the benefit the plan was paying before PBGC trustee the plan, BAPD supplements the BDL with a Benefit Statement, which shows how the benefit was calculated. When an individual requests a BSW, PBGC’s Field Benefit Administration (“FBA”) offices (the Atlanta FBA in the case of the Pilots Plan) produce and mail the BSW. When an individual requests information from PBGC, PBGC’s Disclosure Officer responds to those requests.

The Appeals Board is not directly responsible for providing participants with benefit information. The Appeals Board’s December 21, 2011 letter explained that an individual seeking additional information can request a copy of his or her individual file from PBGC’s Disclosure Officer in accordance with PBGC’s disclosure regulations. At that time, the Disclosure Officer informed the Board that the median time to fulfill these requests was six days. The Board’s May 1, 2012 letter reiterated and clarified statements made in the December 21, 2011 letter.

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<sup>202</sup> See Enclosures 19 and 21.

Since the Appeal's filing on October 28, 2011, PBGC's Disclosure Officer has continued to process the information requests made by your law firm. His office also has processed individual information requests made by Pilots Plan participants, beneficiaries, and alternate payees.

On July 31, 2013, PBGC's Disclosure Officer, Michael L. McIntyre, issued his final response to your firm's disclosure requests. Between October 17, 2012 and July 31, 2013, his office provided your firm with 52,894 pages of documents, which primarily consisted of Delta-originated records and calculations pertaining to your clients.<sup>203</sup>

The Appeal requests that PBGC take actions to remedy the alleged "failures" in PBGC's processes by, at a minimum, reopening the appeal deadline for all appellants while PBGC finishes providing BSWs and other documents to the Pilots Plan's participants and beneficiaries. AB at 48. The Appeals Board denied this request. As stated above, the Disclosure Officer has issued the final response to your information requests. Further, the Board has provided your firm with the opportunity to supplement the Appeal until the Board issues its decision.

The Appeals Board extended the 45-day appeal filing deadline for individuals who timely requested extensions to obtain information from PBGC's Disclosure Officer. In light of the above-discussed PBGC and Appeals Board actions, we found that you and your clients have not been denied the opportunity to evaluate PBGC's benefit determinations and to obtain Appeals Board review.

The Appeals Board's December 21, 2011 letter responded to your request that the Board disclose "any ex parte contacts" with PBGC lawyers concerning the Appeal. As previously stated, the Board does not consider consultations with its attorney-advisers to be ex parte contacts. Furthermore, nothing in ERISA, PBGC's regulations, or policies prohibits the Appeals Board from consulting with its attorney-advisers as part of its deliberations, or requires the Appeals Board to disclose such information.<sup>204</sup>

For the reasons given above and in our December 21, 2011 and May 1, 2012 letters, the Appeals Board denied the Appeal's requests in Issue #12.

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<sup>203</sup> See July 31, 2013 letter from PBGC's Disclosure Officer to  at Enclosure 22.

<sup>204</sup> The Appeal states that the Board's consultation with its attorney-advisers "cannot be squared with the Administrative Procedure Act or due process of law." AB at 48. The Appeal, however, does not cite any specific provision in the Administrative Procedure Act, nor does the Appeal cite any specific legal authority with respect to its due process contention.

**Issue 13: Whether the Appeals Board should grant the Appeal's request for a hearing. AB at 49-50.**

**The Appeal.**

The Appeal initially requested the following:

- (1) An opportunity for individuals with extension requests deemed untimely to present testimony "in order [to] demonstrate 'good cause' for any late filing;"
- (2) An opportunity to present evidence and testimony regarding:
  - a. ALPA Payments of over \$1 billion that were "improperly diverted in violation of Congress' priority scheme" and
  - b. "the classification of these payments as 'pension' payments in other judicial proceedings, including state and federal court filings in which pilots who received these payments classified them as 'pension' payments;"
- (3) An opportunity to present testimony and evidence regarding "[m]aterials and witnesses related to the Delta Bankruptcy proceedings . . . unless, after a review of every filing and transcript in the Bankruptcy proceeding, [the Board] determines that no material disputed facts exist;" and
- (4) An opportunity to present "[m]aterials and witnesses related to the invalidity of the 'Fourth Amendment.' Appellants will submit for testimony Captain [redacted], who will present evidence that in purporting to adopt the Fourth Amendment [to the Plan], Delta did not follow the Plan's amendment procedure as specified in the PWA."

AB at 49. Your hearing request is also addressed in your February 2012 Letter, the AB Supp., your September 2012 Letter, and your May 2013 Letter.

As noted above, the Appeal initially asserted that Captain [redacted] would testify that the Fourth Amendment of the Plan was invalidly adopted. On August 7, 2012, the Appeals Board provided you with documents obtained from ALPA officials that related to the adoption and validity of the Fourth Amendment. After we provided you these materials relating to the Fourth Amendment, you withdrew your request for a hearing to show that the Fourth Amendment was invalid.<sup>205</sup> Accordingly, the Appeal no longer requests a hearing on this issue.<sup>206</sup>

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<sup>205</sup> See Sept. 2012 Letter at 6-9.

<sup>206</sup> The Sept. 2012 Letter states at 8:

Given that the facts . . . suggest that the Fourth Amendment was properly adopted, and moreover that the effective date of the Amendment is irrelevant to the claims at issue in the Consolidated Appeal, Appellants do not believe there are any material facts in dispute in relation to the Fourth Amendment, and withdraw their request for a hearing on this issue.

*Our Response.*

The opportunity for a hearing and the opportunity to present witnesses are permitted at the discretion of the Appeals Board.<sup>207</sup> In general, the Appeals Board will permit an opportunity for a hearing before the Board if the Board determines that there is a dispute as to the material facts.<sup>208</sup>

The Board carefully considered the requests for a hearing in the Appeal. The Board decided that there was not a dispute as to material facts for the following reasons:

- In our December 21, 2011 letter to you, we denied your request for a hearing regarding untimely appeals. We stated that “[t]he Appeals Board has followed PBGC’s regulation in processing appeals, extension requests, and requests for the acceptance of the late-filed appeals.” The Appeals Board offered your clients who failed to meet the 45-day filing rule an opportunity to provide “good cause” why their filing should be considered by the Board.<sup>209</sup>
- Our December 21, 2011 letter also informed your firm that we denied your request for a hearing for the purpose of presenting “materials and witnesses related to the Delta bankruptcy proceedings.” We stated in our letter that the Appeals Board does not intend to review “every filing and transcript” in the Delta bankruptcy proceedings. The Board stated, however, that it would review any submissions of bankruptcy-related materials that you believe are relevant to the issues you raised in the Appeal.
- Your May 2013 letter contains, as an exhibit (Exhibit 2), a transcript of the deposition of [redacted] (“[redacted] Deposition”), which PBGC had provided you in response to your FOIA request. Mr. [redacted] was deposed on May 19, 2006 pursuant to a PBGC discovery request in Delta’s bankruptcy. Consistent with our December 21, 2011 letter, the Appeals Board considered the [redacted] Deposition in reviewing Issue #4.

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The Sept. 2012 Letter states, however, that a hearing “clearly is appropriate” if the Appeals Board changes PBGC’s conclusion that the PWA is a valid plan amendment with an adoption date and a stated effective date that is more than five years before the Pilots Plan’s DOPT. *Id.* at 8-9. Because the Board did not change PBGC’s conclusions with respect to the PWA’s validity, adoption date, and stated effective date (*see* discussions under Issue #1 and Issue #2), there is no need to hold a hearing regarding the PWA.

<sup>207</sup> See 29 C.F.R. § 4003.56.

<sup>208</sup> See 29 C.F.R. § 4003.55.

<sup>209</sup> See Issue #10 of this decision and Enclosure 17.

- The [ ] Deposition was the only supplemental bankruptcy-related document that you submitted with the Appeal. The Board found the [ ] Deposition does not provide a basis for providing relief on any issue in the Appeal.
- The Appeals Board further denied your request to present testimony and evidence regarding how distributions of ALPA Payments to individual pilots are treated “in other judicial proceedings.” This hearing request relates to your Issue #4 claim that PBGC should treat the ALPA Payments as “pension payments” for purposes of the ERISA §§ 4044 and 4022(c) allocations for the Pilots Plan. The Board concluded that testimony and evidence concerning how the ALPA Payments are treated in “other judicial proceedings” is immaterial with regard to your Issue #4 claim.
- In making our decision that no hearing was required, we noted that the scope of the Appeals Board’s authority does not extend to review of positions PBGC takes in litigation (including bankruptcy proceedings), PBGC’s settlement of litigated matters, and PBGC’s decisions concerning whether to seek recovery of funds that may be owed to PBGC-trusted pension plans.<sup>210</sup> Accordingly, we found no reason to provide a hearing with respect to the matters that are outside of the Board’s authority.

In summary, the Board found that there was not a dispute as to material facts in your Appeal; thus, a hearing is not necessary. Therefore, the Board denied your request for a hearing raised in Issue #13.

## **DECISION**

Having applied the Plan’s provisions, the provisions of ERISA, and PBGC’s regulations and policies to the facts in this case, the Appeals Board denied the Appeal with the exception of the following:

- With regard to the Appeal’s request that PBGC conduct another audit of the Pilots Plan’s assets, the Appeals Board confirmed with senior PBGC officials that PBGC has hired a public accounting firm to perform a Plan asset re-evaluation. PBGC will keep Plan participants, beneficiaries, and alternate payees updated on the status of the Plan asset re-evaluation on the [www.pbgc.gov](http://www.pbgc.gov) public website;
- As the Appeal requested, the Board permitted appellants to raise individual appeal issues; and
- The Board corrected errors in the SSA Offset for six appellants, as discussed in Issue #7. For five of the six appellants with SSA Offset errors, the Appeals Board prepared new

<sup>210</sup> See 29 C.F.R. §§ 4003.51 - 4003.61.

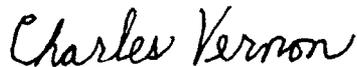
Benefit Statements (Enclosures 11-13 and 15-16 to this decision) that state the corrected benefit amounts determined by the Appeals Board. The Social Security Offset for the sixth appellant ( ) will be corrected when the Board decides his individual appeal.

This decision is PBGC's final Agency action on the Appeal, and all 1,498 appellants may seek review of this decision in an appropriate U.S. District Court.

Thirteen appellants (listed in Enclosure 20) have open individual appeals with the Appeals Board. This decision is not yet PBGC's final Agency action concerning the individual issues raised in the 13 open appeals. The Appeals Board will issue a separate decision to each of these 13 appellants. Finally, two appellants (also listed in Enclosure 20) have an approved extension of time to file an individual appeal. For these two individuals, PBGC's final Agency action will occur when each individual's extension of time expires with no appeal filed or, if an appeal is timely filed, when the appeal is decided.

PBGC will implement final benefit adjustments for all appellants, except those listed in Enclosure 20.<sup>211</sup> If any appellant needs other information regarding his or her PBGC benefits, he or she may contact PBGC's Authorized Plan Representative at 1-800-400-7242.

Sincerely,



Charles Vernon  
Appeals Board Chair

Three Appendices and 22 Enclosures

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<sup>211</sup> Some appellants are receiving the correct PBGC-payable benefit and have no prior overpayments; these appellants will see no change in their monthly payments. Other appellants, however, are currently receiving estimated benefits that are higher than their PBGC-payable benefit (or received higher estimated payments in the past) and have been overpaid by PBGC. PBGC will separately notify these individuals of their new monthly benefit amount and applicable recoupment terms to account for prior overpayments.

## LISTING OF APPENDICES AND ENCLOSURES

### 3 APPENDICES:

- (A) Application of the IRC § 401(a)(17) Limits in Pilots Plan Benefit Calculations (6 pages)
- (B) Delta's Formula Benefit Calculation Methodology (2 pages)
- (C) PBGC's "Percentage Method" for Determining SSA Offset Amounts (8 pages)

### 22 ENCLOSURES:

- (1) List of 1,498 timely-filed appellants (17 pages)
- (2) The 1996 Restatement and its 13 Amendments (179 pages)
- (3) Redacted February 29, 2008 US Airways Appeals Board decision (without Appendices and Enclosures) (43 pages)
- (4) Redacted June 5, 2009 Appeals Board decision addressing the benefits of a US Airways pilot (without Enclosures) (15 pages)
- (5) Transcript of the May 31, 2006 Bankruptcy Court hearing (119 pages)
- (6) PBGC Policy 8.2-1, *Valuation and Allocation of Recoveries*, 5<sup>th</sup> Edition, issued on July 31, 2008 (8 pages)
- (7) Excerpt of the "Retirement Benefits" section of the Pilot Benefits Handbook dated May 1, 1997 and explaining the Minimum Benefit calculation (4 pages)
- (8) The Appeals Board's Sampling of Hard-Copy Appellant Records (15 pages)
- (9) Delta letter sent to a pilot regarding its internal review of SSA Offsets (1 page)
- (10) Delta letters sent to 10 pilots explaining SSA Offset (11 pages)
- (11) Correction of the SSA Offset for [redacted] (5 pages)
- (12) Correction of the SSA Offset for [redacted] (5 pages)
- (13) Correction of the SSA Offset for [redacted] (5 pages)
- (14) Correction of the SSA Offset for [redacted] (1 page)
- (15) Correction of the SSA Offset for [redacted] (5 pages)
- (16) Correction of the SSA Offset for [redacted] (5 pages)
- (17) Explanation of the Appeals Board's processing of appeals and extension requests (7 pages)
- (18) *Your Right to Appeal* pamphlet (8 pages)
- (19) Appeals Board letter to your firm dated December 21, 2011 (4 pages)
- (20) List of Appellants with Open Appeals or Extension Requests (1 page)
- (21) Appeals Board letter to your firm dated May 1, 2012 (4 pages)
- (22) July 31, 2013 letter from PBGC Disclosure Officer, Michael L. McIntyre, to [redacted] (1 page)

## APPENDIX A

### Application of the IRC § 401(a)(17) Limits in Pilots Plan Benefit Calculations

As is explained in Issue #1 of our decision, the Fourth Amendment increased the Pilots Plan's compensation cap to \$200,000 for the "benefit accruals of an Employee in any Plan Year beginning after June 30, 2002."<sup>1</sup> Thus, the Fourth Amendment changed the way that Pilots Plan benefits were computed for pilots who accrued benefits after June 30, 2002 and who later retired or terminated employment. Pilots who retired on July 1, 2002 or earlier, however, are not entitled to benefit increases based on the Amended Compensation Cap because they did not have any benefit accruals on or after July 1, 2002.<sup>2</sup>

In this Appendix A, we provide three examples that describe how the IRC § 401(a)(17) limits are applied in determining a participant's Plan benefit (under the calculation method used by Delta) and PC3 benefit (under PBGC's calculation method).

#### The Pilots Plan's method for computing FAE

Before we present our examples, we explain how the Pilots Plan computed the FAE amount for purposes of determining the Plan's "qualified" benefit.<sup>3</sup> For the basic benefit formula, the Pilots Plan defines FAE as the highest 36-month average over the last 120 months of earnings.<sup>4</sup> Additionally, an IRS regulation provides that, for pension plans that use an average earnings formula, the IRC § 401(a)(17) limits must be applied to 12-month periods of earnings that are used in the average.<sup>5</sup> Delta complied with this IRS regulation by using the following "calendar year" method:<sup>6</sup>

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<sup>1</sup> As stated in the decision, the Fourth Amendment incorporated into the formal Pilots Plan document the agreement that Delta and ALPA previously reached in PWA § 26(G).

<sup>2</sup> The term "Amended Compensation Cap," which is also used in the Issue #1 discussion in the decision, refers to the increased compensation cap that was incorporated into the Pilots Plan's provisions following EGTRRA's enactment.

<sup>3</sup> Delta used earnings above the applicable IRC § 401(a)(17) limits when it calculated the total benefit that a participant was entitled to receive (in combination) from the several pension plans that Delta sponsored. As discussed in the Introduction to this decision, the Delta Pilots Supplemental Annuity Plan ("SAP") paid benefits the Pilots Plan was not permitted to pay due to the IRC § 401(a)(17) limits. PBGC is not responsible for the SAP because it was not a tax-qualified defined benefit pension plan. See ERISA § 4021 (PBGC coverage of tax-qualified defined benefit pension plans).

<sup>4</sup> The 1996 Restatement § 1.17(a).

<sup>5</sup> Treas. Reg. 26 C.F.R. § 1.401(a)(17)-1.

<sup>6</sup> As noted on pages 14-16 of PBGC's Actuarial Case Memo for the Pilots Plan, Delta changed from a "calendar year" method for applying the IRC § 401(a)(17) limits to a "plan year" method starting on January 1, 2003. The Actuarial Case Memo states on page 16:

While this change in method could theoretically result in a decrease in a participant's accrued benefit, no benefit protection as of December 31, 2002 was necessary because a participant's

- i. Delta first determined the 36-month period under which the pilot's average monthly earnings (after application of the IRC § 401(a)(17) limits) were the highest;<sup>7</sup>
- ii. Delta then divided the 36-month period into three consecutive 12-month periods;
- iii. For each of the three 12-month periods, Delta determined the pilot's earnings using the calendar year IRC § 401(a)(17) limit that was in effect when the 12-month period began; and
- iv. Delta completed the FAE calculation by computing the "average" of the three 12-month periods of Earnings.

**Examples of FAE calculations**

Below are qualified FAE calculations for three hypothetical participants. These examples show FAE calculations for the following three situations: (1) a pilot who retired on July 1, 2002, which was one month before the EGTRRA increases went into effect; (2) a pilot who retired on August 1, 2002, which was the first available retirement date after the EGTRRA increase was effective; and (3) a pilot who retired on DOPT-3 (September 2, 2003).

A. Example 1: A pilot who retired on July 1, 2002 (pre-EGTRRA).<sup>8</sup>

In this example, we assume that: (1) the pilot retired on July 1, 2002; (2) his highest 36 months of earnings were from July 1, 1999 to June 30, 2002; and (3) his actual compensation was above the IRC § 401(a)(17) limit during the entire 36-month period.<sup>9</sup>

*FAE for Example 1: Plan benefit calculation.* Using the calendar year method – under which the pilot's earnings are split into three 12-month periods – Delta would compute this pilot's monthly "qualified" FAE as \$13,888.89 (\$166,666.67 as an annual amount). This calculation is shown in the table below:

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accrued benefit was unaffected until January 1, 2005. Thus, we considered the calendar year method part of the 5- and 4-year-old plan provisions and the plan year method part of the plan provisions during the 3-year period before DOPT.

The Pilots Plan's change from the "calendar year" method to the "plan year" method does not impact how benefits in PC3 are determined.

<sup>7</sup> Plan § 1.17(c) provides that, if a pilot had Earnings in a month that were less than 75% of his average Earnings during the calendar year, that month would not be included as one of the 36 months of highest Earnings. Instead, the next "contiguous month" that equaled or exceeded 75% of his average Earnings during the calendar year would be included in the 36-month period. Delta and PBGC applied this 75% rule in determining the pilot's FAE.

<sup>8</sup> Example 1 could also apply to a pilot who retired earlier than July 1, 2002.

<sup>9</sup> This example is similar to the example set forth on page 16 of PBGC's Actuarial Case Memo.

<b>Example 1: FAE used for Plan benefit calculation (pilot retired 7/1/2002)</b>	
<b>12-month earnings period</b>	<b>IRC § 401(a)(17) limit applied</b>
7/1/1999 – 6/30/2000	\$160,000 (1999)
7/1/2000 – 6/30/2001	\$170,000 (2000)
7/1/2001 – 6/30/2002	\$170,000 (2001)
Total for 3 years (36 months)	\$500,000
<b>\$500,000 ÷ 36 = \$13,888.89 (monthly FAE)</b>	

*FAE for Example 1: PC3 benefit calculation.* For pilots who retired on or before July 1, 2002, the FAE is the same for both PC3 and Plan benefit amounts because they both are calculated based on Pilots Plan's provisions that were in effect more than 5 years before DOPT. Thus, for this example, the monthly FAE that PBGC uses in the participant's PC3 benefit calculation (\$13,888.89) is the same monthly FAE that is used in the Plan benefit calculation. We show this in the table below.

<b>Example 1: FAE used for PC3 benefit calculation (pilot retired 7/1/2002)</b>	
<b>12-month earnings period</b>	<b>IRC § 401(a)(17) limit applied</b>
7/1/1999 – 6/30/2000	\$160,000 (1999)
7/1/2000 – 6/30/2001	\$170,000 (2000)
7/1/2001 – 6/30/2002	\$170,000 (2001)
Total for 3 years (36 months)	\$500,000
<b>\$500,000 ÷ 36 = \$13,888.89 (monthly FAE)</b>	

B. Example 2: A pilot who retired on August 1, 2002 (EGTRRA applies to Plan benefit only).

In this example, we assume that the pilot retired on August 1, 2002, which was one month later than the pilot in Example 1. Similar to the first example, in Example 2 we assume that: (1) his highest 36 months of earnings were from August 1, 1999 to July 31, 2002, and (2) his actual compensation was above the IRC § 401(a)(17) limits during the entire 36-month period.

*FAE for the Example 2: Plan benefit calculation.* Although Delta used the calendar year method (as in Example 1), if a pilot had any earnings on or after July 1, 2002, Delta applied the \$200,000 EGTRRA limit retroactively to all earnings before July 1, 2002 (as provided under the Fourth Amendment). Accordingly, because this pilot had earnings after July 1, 2002, the \$200,000

EGTRRA limit applies to all his earnings. Thus, under Delta's method, this pilot's monthly FAE for purposes of calculating his Pilots Plan benefit amount is \$16,666.67 (\$200,000 as an annual amount). This calculation is shown in the table below:

<b>Example 2: FAE used for Plan benefit calculation (pilot retired 8/1/2002)</b>	
<b>12-month earnings period</b>	<b>IRC § 401(a)(17) limit applied</b>
8/1/1999 – 7/31/2000	\$200,000 (EGTRRA)
8/1/2000 – 7/31/2001	\$200,000 (EGTRRA)
8/1/2001 – 7/31/2002	\$200,000 (EGTRRA)
Total for 3 years (36 months)	\$600,000
<b>\$600,000 ÷ 36 = \$16,666.67 (monthly FAE)</b>	

*FAE for Example 2: PC3 benefit calculation.* In Example 2, the FAE is significantly lower for the PC3 benefit than for the Plan benefit because the PC3 benefit is based on the Pilots Plan's provisions in effect more than 5 years before DOPT (i.e., at DOPT-5), which did not include the Amended Compensation Cap.

For the PC3 benefit, PBGC applies the applicable (pre-EGTRRA) limit under IRC § 401(a)(17) for each 12-month earnings period that starts before DOPT-5. For instance, the 1999 IRC § 401(a)(17) limit of \$160,000 applies to the 12-month period between August 1999 and July 2000, because that was the applicable IRC § 401(a)(17) limit at the start of the 12-month earnings period. If the pilot had a 12-month earnings period after the EGTRRA IRC § 401(a)(17) limit of \$200,000 went into effect for the Pilots Plan (i.e., a 12-month period of earnings beginning on or after July 1, 2002), PBGC caps the earnings for PC3 purposes at \$170,000, the IRC § 401(a)(17) limit in effect at DOPT-5 (September 2, 2001).

As is shown in the table below, the monthly FAE that PBGC uses in the PC3 benefit calculation for the pilot in Example 2 is \$13,888.89. We note that the pilot in Example 2 has the same FAE for PC3 benefit purposes as the participant in Example 1, who retired only one month earlier.

<b>Example 2: FAE used for PC3 benefit calculation (pilot retired 8/1/2002)</b>	
<b>12-month earnings period</b>	<b>IRC § 401(a)(17) limit applied</b>
8/1/1999 – 7/31/2000	\$160,000 (1999)
8/1/2000 – 7/31/2001	\$170,000 (2000)
8/1/2001 – 7/31/2002	\$170,000 (2001)
Total for 3 years (36 months)	\$500,000
<b>\$500,000 ÷ 36 = \$13,888.89 (monthly FAE)</b>	

C. Example 3: A pilot who retired October 1, 2003 (the first available retirement date after DOPT-3) (EGTRRA applies to Plan benefit only)

In this example, we assume that the pilot ended his Delta employment on DOPT-3 (September 2, 2003) and retired on the first day of the next month (i.e., October 1, 2003). Similar to the prior two examples, we assume in Example 3 that: (1) his highest 36 months of earnings were from September 1, 2000 to August 31, 2003,<sup>10</sup> and (2) his actual compensation was above the IRC § 401(a)(17) limits during the entire 36-month period.

*FAE for the Example 3: Plan benefit calculation.* As is the case with Example 2, Delta applied the \$200,000 EGTRRA limit retroactively to earnings before July 1, 2002 (as provided under the Fourth Amendment) for this participant. This participant retired before any COLA increases to the \$200,000 EGTRRA limit went into effect. Accordingly, under Delta's method, this pilot's monthly FAE for purposes of calculating his Pilots Plan benefit amount is \$16,666.67 (\$200,000 as an annual amount), which is the same as in Example 2. This calculation is shown in the table below:

<b>Example 3: FAE used for Plan benefit calculation (pilot retired 10/1/2003)</b>	
<b>12-month earnings period</b>	<b>IRC § 401(a)(17) limit applied</b>
9/1/2000 – 8/31/2001	\$200,000 (EGTRRA)
9/1/2001 – 8/31/2002	\$200,000 (EGTRRA)
9/1/2002 – 8/31/2003	\$200,000 (EGTRRA)
Total for 3 years (36 months)	\$600,000
<b>\$600,000 ÷ 36 = \$16,666.67 (monthly FAE)</b>	

*FAE for the Example 3: PC3 benefit calculation.* The FAE for the PC3 benefit is larger in Example 3 than in Examples 1 and 2. This occurs because the pre-EGTRRA limit of \$170,000 – which is the cap under the Plan's provisions in effect at DOPT-5 – applies to all three years of the pilot's earnings in Example 3, but to only the last two years of earnings in Example 1 and 2. In Example 3, the FAE that PBGC uses in the participant's PC3 benefit calculation is \$14,166.67. This calculation is shown in the table below:

<sup>10</sup> Although the pilot worked one day in September 2003, we assume that his earnings on that day did not make September 2003 one of his highest 36 months of earnings.

<b>Example 3: FAE used for PC3 benefit calculation (pilot retired 10/1/2003)</b>	
<b>12-month earnings period</b>	<b>IRC § 401(a)(17) limit applied</b>
9/1/2000 – 8/31/2001	\$170,000 (2000)
9/1/2001 – 8/31/2002	\$170,000 (2001)
9/1/2002 – 8/31/2003	\$170,000 (capped at DOPT-5 limit)
<b>Total for 3 years (36 months)</b>	<b>\$510,000</b>
<b><math>\\$510,000 \div 36 = \\$14,166.67</math> (monthly FAE)</b>	

The FAE used in a pilot's PC3 benefit calculation ordinarily will not exceed the \$14,166.67 monthly amount (\$170,000 as an annual amount) shown in Example 3, even if the pilot retired after October 1, 2003.<sup>11</sup> This is because, for PC3 purposes, the pilot is assumed to have retired at DOPT-3. Thus, for PC3, earnings after September 2, 2003 cannot be used to calculate the pilot's FAE. Furthermore, because the PC3 benefit is computed using the plan provisions in effect during the 5 years before plan termination, the pilot's FAE is capped at \$170,000 (annually) even if he retires after DOPT-3.

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<sup>11</sup> As stated in Issue #1 of the decision, the Pilots Plan's provisions, both before and after EGTRRA, contain a special rule that applies to pilots who have pre-1996 earnings that are limited by the more generous \$200,000 compensation cap (plus COLAs) in effect prior to OBRA '93. The examples in this Appendix A assume that the pilot's FAE under the generally-applicable rule is greater than the pilot's benefit under the special rule.

## **APPENDIX B**

### **Delta's Formula Benefit Calculation Methodology**

For Participants eligible for the Minimum Benefit, Delta's calculation methodology is as follows:

- Delta first calculated the "Formula Benefit" under Plan § 1.18. The Formula Benefit is the benefit amount, expressed as a monthly Single Life Annuity ("SLA") at age 60, that is the greater of the total benefit under the FAE formula and the total benefit under the Minimum Benefit formula with no IRC § 401(a)(17) earnings limits applied to monthly earnings. The Formula Benefit is reduced for early commencement under Plan § 1.18.
- If the Formula Benefit is greater under the Minimum Benefit formula, then no Social Security Administration offset ("SSA Offset") is applied.<sup>1</sup> If the greater Formula Benefit is under the FAE formula, then a SSA Offset is applied at the earlier of age 65 or when a participant begins receiving Social Security retirement, consistent with Plan § 5.03.
- At retirement (and before Delta determined how much of the Formula Benefit is a qualified benefit), one-half of the Formula Benefit is allocated to the participant's Variable Benefit and the remaining one-half is allocated to the participant's Fixed Annuity Benefit.
- Delta next calculated the "Preliminary Qualified Benefit" as the greater of the benefit under the FAE formula and the benefit under the Minimum Benefit formula after applying the IRC § 401(a)(17) limit (i.e., using "qualified" earnings capped by the IRC § 401(a)(17) limit). If a participant's earnings exceeded the IRC § 401(a)(17) limit—which they often did—the Preliminary Qualified Benefit was less than the total Formula Benefit, and the difference was payable by the Supplemental Annuity Plan ("SAP"). By calculating the Preliminary Qualified Benefit as the greater of the benefit under the FAE formula and the benefit under the Minimum Benefit formula (after applying the IRC § 401(a)(17) limit), Delta ensured that a participant's qualified benefit was maximized and the amount of nonqualified benefit assigned to the SAP was minimized. This Delta practice was also consistent with the Plan's requirement that the participant's benefit is no less than the qualified benefit under the Minimum Benefit formula.
- Delta calculated the IRC § 415(b) monthly benefit limit applicable to the participant based on his or her age and retirement date. The IRC § 415 limit, if applicable, reduced the Preliminary Qualified Benefit to the Plan's final qualified benefit. If the Preliminary Qualified Benefit is reduced to a lower final qualified

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<sup>1</sup> See Plan § 8.02.

benefit by the IRC § 415 limit, the nonqualified portion of the Preliminary Qualified Benefit would be paid from the Bridge Plan.

- After the final tax-qualified benefit was calculated, Delta determined how much of the Variable and Fixed Benefits are payable as a tax-qualified benefit. Often, a significant portion of the Fixed Benefit consisted of nonqualified benefits. Plan provisions dictate which parts of the nonqualified benefit would be paid by the SAP and the Bridge Plan.
- Delta (and, after DOPT, PBGC) reduced the qualified benefit by the SSA Offset for retired pilots whose Formula Benefit was greater under the FAE formula.<sup>2</sup> The SSA Offset is applied at age 65 or an earlier date if the pilot commenced Social Security benefits before age 65.

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<sup>2</sup> We found numerous examples showing that the Pilots Plan's practice was to first apply the SSA Offset to the Bridge Plan benefit before reducing the tax-qualified benefit. For pilots who did not have a Bridge Plan benefit, Delta applied the SSA Offset immediately to the tax-qualified benefit. PBGC continued this practice after DOPT, which is favorable to appellants.

## APPENDIX C

### PBGC's "Percentage Method" for Determining SSA Offset Amounts

As stated in the decision, for some appellants the PBGC-payable benefit amount is the same as the Plan benefit amount; PBGC applies the same SSA Offset as prescribed by the Plan for these appellants.<sup>1</sup>

For many appellants with the SSA Offset, however, the PBGC-payable benefit is less than the Plan benefit. For these individuals, PBGC uses a "Percentage Method" to calculate the SSA Offset applicable to the individual's PBGC-payable benefit. Under the Percentage Method, the SSA Offset applied by PBGC to the PBGC-payable benefit is reduced in proportion to the reduction in the individual's Plan benefit.

In the decision, the Board concluded that PBGC did not err in applying the Percentage Method in determining the SSA Offset reductions to appellants' PBGC-payable benefits.

In this Appendix, we explain the Percentage Method in detail. First, we provide a general explanation of PBGC's six calculation steps under the Percentage Method. This is followed by a detailed explanation of how PBGC applied the Percentage Method to the two appellants discussed in the decision, [redacted] and [redacted].

#### General Explanation of Percentage Method

Pilots Plan participants often have non-level benefits because the SSA Offset to their benefits does not begin immediately (e.g., the Pilots Plan benefit may start at age 60 with the reduction for the SSA Offset starting at age 65). When the PBGC-payable benefit amounts are non-level and less than the Plan benefit amounts, PBGC uses a "Percentage Method" to calculate PBGC-payable benefit amounts.<sup>2</sup>

Under the Percentage Method, an individual's PBGC-payable non-level benefit amounts will equal a percentage (based on present values) of the individual's non-level plan benefit amounts. PBGC does not limit its use of the Percentage Method to the SSA Offset; PBGC also applies it when benefits are non-level for other reasons. The explanation below, however, applies only to the SSA Offset under the Pilots Plan.

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<sup>1</sup> The "Plan benefit" is the benefit PBGC would pay if the Pilots Plan had been fully funded.

<sup>2</sup> If the individual's non-level PBGC-payable benefit amounts equal the individual's non-level Plan benefit amounts, then PBGC applies a percentage of 100% (i.e., there will be no reduction to the Plan benefit amounts).

For Plan participants and beneficiaries impacted by the SSA Offset, PBGC applies the following six steps in determining the individual's PBGC-payable benefit:

- i. PBGC's first step is to calculate monthly PC3 and Plan benefits based on the Plan's provisions. We refer to the monthly PC3 amounts that PBGC first computes as the "Preliminary PC3 Benefit." The start date and amount of the SSA offset generally will be the same for the Preliminary PC3 Benefit and for the Plan benefit.
- ii. PBGC next determines the "percentage" of the individual's funded PC3 benefit in comparison to his or her Plan benefit ("PC3 %"). To accomplish this, PBGC: (1) for both the Preliminary PC3 Benefit and Plan benefit, converts the monthly amounts payable after DOPT to present values based on PBGC's valuation assumptions for the Plan;<sup>3</sup> (2) adjusts the PC3 benefit present value for the Pilots Plan's PC3 funding percentage of 93.03847%; and (3) divides the present value of the funded PC3 benefit by the present value of the Plan benefit, which yields the PC3 %.
- iii. PBGC then applies a similar procedure to determine the "percentage" of the individual's Plan benefit amount that is guaranteed (after adjustment for any lump sum distribution) ("guarantee %").<sup>4</sup>
- iv. PBGC's fourth step is to use the greater of the individual's PC3 % and guarantee % for purposes of determining the PBGC-payable benefit before considering the ERISA § 4022(c) amount (if any). PBGC uses the term "Title IV benefit" in referring to the benefit payable before the ERISA § 4022(c) amount. The monthly (non-level) Title IV amounts computed in this step equal a percentage of the individual's monthly (non-level) Plan benefit amounts. The impact of this calculation is that the SSA Offset is reduced in proportion to the reduction in the individual's Plan benefit amounts.<sup>5</sup>

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<sup>3</sup> For the Pilots Plan, PBGC applied the Appendix B interest rates in effect on the Pilots Plan's September 2, 2006 termination date, which are 6.20% for 20 years and 4.75% thereafter. See 29 C.F.R. § 4044.75 Appendix B to Part 4044, "Interest Rates Used to Value Benefits." PBGC also used the mortality assumptions prescribed in PBGC's regulation at 29 C.F.R. § 4044.53.

<sup>4</sup> For this computation, PBGC determines the "level" value of the MGB using the factors set forth in PBGC regulation 29 C.F.R. § 4022.23, rather than PBGC's valuation assumptions for the Plan.

<sup>5</sup> For example, if the individual's guarantee % is 40% and his PC3 % is 60%, the Title IV benefit amounts will equal 60% (the larger percentage) of the individual's Plan benefit amounts. We also will assume in this example that this individual's Plan benefit is \$4,116.65 before an age-65 SSA Offset of \$116.65 and \$4,000.00 starting at age 65. This individual's Title IV benefit will be \$2,469.99 before the SSA Offset [ $\$4,116.65 \times 60\% = \$2,469.99$ ] and \$2,400.00 starting at age 65 [ $\$4,000 \times 60\% = \$2,400.00$ ]. We note that, in this example, the SSA Offset to the PBGC-payable benefit is 60% of the SSA Offset to the Plan benefit or \$69.99 [ $\$116.65$  (SSA Offset to Plan benefit)  $\times 60\% = \$69.99$ ].

- v. PBGC next determines the individual's ERISA § 4022(c) amounts. PBGC computes ERISA § 4022(c) amounts as a percentage of the Plan benefit the individual is entitled to receive. For some appellants (such as Mr. [ ] and Mr. [ ]), the ERISA § 4022(c) amount effectively will provide them with 100% of their PC3 benefit, but will not fund their benefits in PC5.<sup>6</sup> The ERISA § 4022(c) amount also funds a portion of the PC5 benefit for some other appellants (i.e., appellants who worked for Delta after DOPT-3), in addition to effectively providing them with 100% of their PC3 benefit.
- vi. The final (sixth) step is to add the ERISA § 4022(c) amounts to the Title IV amounts, which results in the total monthly PBGC-payable benefit.

Application of Percentage Method to Appellant [ ]

The following explains PBGC's Percentage Method calculations for appellant [ ]. Mr. [ ] is one of three individuals you identified in Appeal Exhibit 31.

Mr. [ ] was born October 22, 1942. His seniority date for Delta was November 4, 1968, and he retired on November 1, 2002. He elected to receive a Straight Life Annuity benefit with his variable annuity as a lump-sum distribution (paid at his retirement). Mr. [ ]'s total Formula Benefit was highest under the FAE formula, not the Minimum Benefit formula. Thus, the SSA Offset applies to his benefit.

Because Mr. [ ]'s seniority date is prior to February 9, 1982, his Primary Social Security Benefit is equal to \$233.30. Using the Pilots Plan § 5.03 formula, the Plan's SSA offset at age 65 is \$116.65 [ $50\% \times \text{Primary Social Security Benefit} \times \text{Years of Service up to 25} \div 25 = 0.50 \times \$233.30 \times 25 \div 25$ ].

As shown in lines (158) and (159) of his BSW, PBGC determined that Mr. [ ]'s PBGC-payable benefit is: \$3,870.45 before age 65 and \$3,764.29 starting at age 65. The calculation of those amounts is explained below:

- PBGC's first step is to calculate Mr. [ ]'s monthly Preliminary PC3 Benefit and his monthly Plan benefit in accordance with the Pilots Plan's provisions. PBGC calculated his Preliminary PC3 Benefit amounts as \$3,879.93 before age 65 and \$3,763.28 starting at age 65. PBGC calculated his Plan benefit amounts as \$4,252.81 before age 65 and \$4,136.16 starting at age 65. For both his Preliminary PC3 Benefit and his Plan benefit, his SSA Offset is \$116.65 beginning at age 65.

<sup>6</sup> Mr. [ ], Mr. [ ], and other similarly-situated participants will not receive a portion of their ERISA § 4022(c) amount as a PC5 benefit because they are not entitled to a benefit in the PC5(a) subcategory, and the Plan's ERISA § 4022(c) amounts were exhausted before reaching benefits in the PC5(b) subcategory. See explanation under Issue #5.B.

- PBGC next made present value calculations to determine the PC3 % (i.e., the “percentage” of Mr. [ ]’s funded PC3 benefit in comparison to his Plan benefit). For Mr. [ ], the PC3 % is 84.67347%.
- PBGC then applied its similar procedure to determine the guarantee % (i.e., the percentage” of the Plan benefit amount that is guaranteed (after adjustment for any lump sum distribution)). For Mr. [ ], the value of his lump sum exceeded his guaranteed benefit amount, and, accordingly, his guarantee % is 0%.
- PBGC’s fourth step is to use the greater of the individual’s PC3 % and guarantee % for purposes of determining the Title IV benefit (i.e., the PBGC-payable benefit before the ERISA § 4022(c) amount (if any)). For Mr. [ ], PBGC multiplied his PC3 % of 84.67347% (which exceeded his guarantee % of 0%) by his Plan benefit amounts. This results in Title IV benefit amounts of \$3,601.00 before age 65 [ $\$4,252.81 \times 84.67347\% = \$3,601.00$ ] and \$3,502.23 starting at age 65 [ $\$4,136.16 \times 84.67347\% = \$3,502.23$ ].
- PBGC then computed Mr. [ ]’s ERISA § 4022(c) amounts, which (like his Title IV benefit) is a percentage of his Plan benefit. PBGC determined that Mr. [ ]’s monthly ERISA § 4022(c) amount equaled 6.33572% of his Plan benefit amount. Therefore, his monthly ERISA § 4022(c) benefit is (i) \$269.45 before age 65 [ $\$4,252.81 \times 6.33572\% = \$269.45$ ] and (ii) \$262.06 starting at age 65 [ $\$4,136.16 \times 6.33572\% = \$262.06$ ].
- The final (sixth) step is to add the ERISA § 4022(c) amounts to the Title IV amounts, which result in the total monthly PBGC-payable benefit. For Mr. [ ], his monthly PBGC-payable benefit is: \$3,870.45 before age 65 [ $\$3,601.00$  (Title IV amount) + \$269.45 (ERISA § 4022(c) amount) = \$3,870.45] and \$3,764.29 starting at age 65 [ $\$3,502.23$  (Title IV amount) + \$262.06 (ERISA § 4022(c) amount) = \$3,764.29]. Each of those two amounts is 91.01% of the corresponding Plan benefit amount. Consequently, the SSA Offset under the Percentage Method is \$106.16, which is 91.01% of the SSA Offset in the Plan benefit calculation.

The table below, prepared by the Board, shows PBGC's calculations for Mr. [redacted].

**How Mr. [redacted]'s PBGC-payable Benefit is Determined**

		Present Value of Benefit at DOPT	(I) Monthly Benefit Amount Before SSA Offset	(II) Monthly Benefit Amount After SSA Offset on 11/01/2007 at Age 65	Monthly SSA Offset [(I) - (II)]
A	Plan Benefit	\$543,900	\$4,252.81	\$4,136.16	\$116.65
B	Preliminary PC3 Benefit	\$494,999	\$3,879.93	\$3,763.28	\$116.65
C	Present Value of PC3 Benefit Funded by Plan Assets [(B) × 93.03847%]	\$460,539			
D	The PC3 % (i.e., the percentage of the funded PC3 Benefit compared to the Plan Benefit) [(C) ÷ (A)]	84.67347%			
E	Title IV Monthly Benefit [(A) × (D)]	\$460,539	\$3,601.00	\$3,502.23	\$98.77
F	Present Value of ERISA § 4022(c) Benefit (i.e., present value of PC3 Benefit not funded by Plan Assets, since there is no benefit payable in PC5) [(B) - (C)]	\$34,460			
G	% of Plan Benefit Funded by ERISA § 4022(c) [(F) / (A)]	6.33572%			
H	ERISA § 4022(c) Benefit [(A) × (G)]	\$34,460	\$269.45	\$262.06	\$7.39
<b>I</b>	<b>PBGC Benefit [(E) + (H)]</b>		<b>\$3,870.45</b>	<b>\$3,764.29</b>	<b>\$106.16</b>

The Appeals Board found that the Percentage Method adjustments for Mr. [redacted] do not decrease the actuarial value of the Preliminary PC3 benefit amounts PBGC calculated, and, accordingly, do not result in a financial gain to PBGC.

*Application of Percentage Method to Appellant [redacted]*

Mr. [redacted] was born [redacted], 1948. His seniority date for Delta was [redacted] 1977, and he retired on [redacted], 2003. Mr. [redacted] elected to receive his Variable Annuity as a lump-sum distribution and his Fixed Annuity as a Straight Life Annuity benefit. Mr. [redacted]' total

Formula Benefit was highest under the FAE formula, not the Minimum Benefit formula. Thus, the SSA Offset applies to his benefit.

Because Mr. [ ]'s seniority date is prior to February 9, 1982, his Primary Social Security Benefit is equal to \$233.30. Using the Pilots Plan § 5.03 formula, his SSA Offset at age 65 under the Plan is \$116.65 [ $50\% \times \text{Primary Social Security Benefit} \times \text{Years of Service up to } 25 \div 25 = 0.50 \times \$233.30 \times 25 \div 25$ ].

The amounts stated in PBGC's June 2010 benefit determination are based on the assumption that Mr. [ ] would not commence Social Security benefits before age 65. As shown in lines (158) and (159) of his BSW, PBGC determined that Mr. [ ]'s PBGC-payable benefit is: \$1,653.38 before age 65 and \$1,588.85 starting at age 65. In the explanation below, we discuss the benefit amounts that PBGC initially determined for Mr. [ ] based on an age 65 start date of his SSA Offset.

- PBGC's first step is to calculate Mr. [ ]'s monthly Preliminary PC3 Benefit and his monthly Plan benefit in accordance with the Pilots Plan's provisions. PBGC calculated his Preliminary PC3 Benefit amounts as \$1,683.52 before age 65 and \$1,566.87 starting at age 65. PBGC calculated his Plan benefit amounts as \$2,988.52 before age 65 and \$2,871.87 starting at age 65. For both his Preliminary PC3 Benefit and his Plan benefit, his SSA Offset is \$116.65 beginning at age 65.
- PBGC's next made present value calculations to determine the PC3 % (i.e., the "percentage" of Mr. [ ]'s funded PC3 benefit in comparison to his Plan benefit). For Mr. [ ], the PC3 % is 51.47298%.
- PBGC then applied its similar procedure to determine the guarantee % (i.e., the "percentage" of the Plan benefit amount that is guaranteed (after adjustment for any lump sum distribution)). For Mr. [ ], the value of his lump sum exceeded his guaranteed benefit amount, and, accordingly, his guarantee % is 0%.
- PBGC's fourth step is to use the greater of the individual's PC3 % and guarantee % for purposes of determining the Title IV benefit (i.e., the PBGC-payable benefit before the ERISA § 4022(c) amount (if any)). For Mr. [ ], PBGC multiplied his PC3 % of 51.47298% (which exceeded his guarantee % of 0%) by his Plan benefit amounts. This results in Title IV benefit amounts of \$1,538.28 before age 65 [ $\$2,988.52 \times 51.47298\% = \$1,538.28$ ] and \$1,478.24 starting at age 65 [ $\$2,871.87 \times 51.47298\% = \$1,478.24$ ].
- PBGC then computed Mr. [ ]'s ERISA § 4022(c) amounts, which (like his Title IV benefit) is a percentage of his Plan benefit. PBGC determined that Mr. [ ]'s monthly ERISA § 4022(c) amount equaled 3.85145% of his Plan benefit amount. Therefore, his monthly ERISA § 4022(c) benefit is (i) \$115.10 before age 65 [ $\$2,988.52 \times 3.85145\% = \$115.10$ ] and (ii) \$110.61 starting at age 65 [ $\$2,871.87 \times 3.85145\% = \$110.61$ ].

- The final (sixth) step is to add the ERISA § 4022(c) amounts to the Title IV amounts, which result in the total monthly PBGC-payable benefit. For Mr. [redacted], his monthly PBGC-payable benefit is: \$1,653.38 before age 65 [\$1,538.28 (Title IV amount) + \$115.10 (ERISA § 4022(c) amount) = \$1,653.38] and \$1,588.85 starting at age 65 [\$1,478.24 (Title IV amount) + \$110.61 (ERISA § 4022(c) amount) = \$1,588.85]. Each of those two amounts is 55.32% of the corresponding Plan benefit amount. Consequently, the SSA Offset under the Percentage Method is \$64.53, which is 55.32% of the SSA Offset in the Plan benefit calculation.

The table below, prepared by the Board, shows PBGC's calculations for Mr. [redacted].

**How Mr. [redacted]' PBGC-payable Benefit is Determined**

		Present Value of Benefit as of DOPT	(I) Monthly Benefit Amount Before SSA Offset	(II) Monthly Benefit Amount After SSA Offset on 01/01/2013 at Age 65	Monthly SSA Offset [(I) - (II)]
A	Plan Benefit	\$425,736	\$2,988.52	\$2,871.87	\$116.65
B	Preliminary PC3 Benefit	\$235,536	\$1,683.52	\$1,566.87	\$116.65
C	Present Value of PC3 Benefit Funded by Plan Assets [(B) × 93.03847%]	\$219,139			
D	The PC3 % (i.e., the percentage of the funded PC3 Benefit compared to the Plan Benefit) [(C) ÷ (A)]	51.47298%			
E	Title IV Monthly Benefit [(A) × (D)]	\$219,139	\$1,538.28	\$1,478.24	\$60.04
F	Present Value of ERISA § 4022(c) Benefit (i.e., present value of PC3 Benefit not funded by Plan Assets, since there is no benefit payable in PC5) [(B) - (C)]	\$16,397			
G	% of Plan Benefit Funded by ERISA § 4022(c) [(F) ÷ (A)]	3.85145%			
H	ERISA § 4022(c) Benefit [(A) × (G)]	\$16,397	\$115.10	\$110.61	\$4.49
I	<b>PBGC Benefit [(E) + (H)]</b>		<b>\$1,653.38</b>	<b>\$1,588.85</b>	<b>\$64.53</b>

The Appeals Board found that the Percentage Method adjustments for Mr. [ ] do not decrease the actuarial value of the Preliminary PC3 benefit amounts PBGC calculated, and, accordingly, do not result in a financial gain to PBGC.

After PBGC issued its benefit determination, Mr. [ ] notified PBGC of his Social Security benefit commencement. PBGC started applying a SSA Offset on October 1, 2010 (27 months prior to his age 65). PBGC, in accordance with the Pilots Plan's terms, reduced the SSA Offset amount based on his early Social Security benefit commencement date. The table below shows Mr. [ ]' actual PBGC-payable benefit and his actual SSA Offset effective October 1, 2010.<sup>7</sup>

<b>Actual PBGC Benefit after adjusting for Mr. [ ]' early SSA benefit commencement</b>	<b>\$1,653.38 Prior to Oct. 1, 2010</b>	<b>\$1,598.55 on and after Oct. 1, 2010</b>	<b>\$54.83 SSA Offset</b>
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<sup>7</sup> Under the Pilots Plan's provisions, the SSA Offset is reduced by 5/9 of 1% for each month the Social Security benefit commencement date precedes age 65. See Social Security Handbook at [http://www.ssa.gov/OP\\_Home/handbook](http://www.ssa.gov/OP_Home/handbook). Because Mr. [ ] commenced his Social Security benefits on [ ] (27 months before age 65), his SSA Offset is reduced to 85% of the full offset amount [100% - (27 months early × 5/9% per month reduction) = 85%]. Thus, for his PBGC-payable benefit, the Board found that his SSA Offset reduced for his early Social Security benefit commencement should be \$54.85 [\$64.53 (age-65 SSA Offset) × 0.85 = \$54.85 (SSA Offset starting 1/1/2010)]. PBGC calculated his SSA Offset as \$54.83. The Board is not changing Mr. [ ]' PBGC-payable benefit based on this \$0.02 difference, which is favorable to him.