

Pension Benefit Guaranty Corporation

76-88

June 25, 1976

REFERENCE:

[*1] 4062(a) Liability of Employer in Single Employer Plans. Applicability
4062(b) Liability of Employer in Single Employer Plans. Amount of Employer Liability
4063 Liability of Substantial Employer for Withdrawal

OPINION:

* * * of the Pension Benefit Guaranty Corporation ("PBGC"), asked this Pension Office to reply to your letter posing a series of questions concerning your company's potential liability under Section 4062(b) of the Employee Retirement Income Security Act of 1974 (the "Act") in connection with the possible underfunding of the pension plan (the "Plan") that * * * has adopted pursuant to an agreement with the * * *

1. Based on a review of the Plan document, we have determined that the Plan is a defined benefit plan inasmuch as it promises a defined benefit at retirement. The Plan provides a monthly benefit of \$7.00 times an employee's years of continuous service, up to a 35-year maximum. Pursuant to Section 4021(a) of the Act, a tax-qualified pension plan is covered under Title IV of the Act unless it is exempt under Section 4021(b). Your inquiry suggests that you think the Plan might be exempt under Section 4021(b)(1), as an individual account plan. The term "individual [*2] account plan" or "defined contribution plan" refers to those types of employee benefit plans where retirement benefits are determined solely by reference to the amount accumulated in each participant's account. Most other pension plans are defined benefit plans. See Act, Sections 3(34) and 3(35). Clearly the Plan is not an individual account plan since benefits are not based on the amount in a participant's account. The classification of a plan as a defined benefit plan is determined by the benefit the plan promises its participants, not by the plan's provisions relating to the employer's obligation to the plan.

2. Although the Plan in which your employees participate * * * covers employees of other companies in the * * * area that have entered into collective agreements with the * * *, the Plan is not a "multiemployer plan" as that term is used in the Act. This conclusion is based on the fact that participants' rights to benefits under the Plan are substantially affected by their employer's cessation of contributions. See Section 414(g)(1) (D) of the Internal Revenue Code, Act § 41014. Thus if the plan terminates as to your company, the company would be liable to the PBGC [*3] under Section 4062(b) of the Act as an employer that maintained a single-employer plan, rather than as an * * * employer that maintained a single-employer plan, rather than as an employer withdrawing from a multiple employer plan * * * under Section 4063 of the Act.

Your company's potential liability can be calculated in the following manner:

That portion of Plan assets applicable to * * * under Article X of the Plan, and the benefit obligations running to present and former employees of * * * are treated as a separate plan that terminates on the date * * * ceases participation in the original Plan * * * (unless * * * maintains its portion of the Plan independently, beyond that date). If your Plan terminates, its assets must be allocated to the participants' benefits in accordance with the priority schedule set forth in Section 4044 of the Act. Under that allocation scheme, retired participants' benefits will be in priority categories 3, 4, and possibly, category 5. Some active participants with vested rights will also have benefits in categories 3, 4 and possibly 5. * * * The assets of * * * separate plan must be used to satisfy all the priority category 3 benefits before they [*4] may be used to cover lower priority benefits.

Under Article X of the Plan, the Plan has a qualified obligation to fund the benefits being paid to retirees, even after their former employer ceases participation in the Plan. If the assets of * * * separate plan, after allocation in compliance with Section 4044 of the Act, do not cover all the benefits to which retired * * * employees are entitled, the Plan is liable to those retirees for the remainder of their benefits. Liability for the benefits that the Plan is continuing to pay to retired * * * employees would not be included in the PBGC's computation of the current value of the benefits guaranteed by the PBGC on the date of termination, because the Plan's continuing obligation in effect satisfies that liability. *

* It might be advisable to consult the Department of Labor and the Internal Revenue Service to determine whether Sections 208 of ERISA and 401(a)(12) of the Internal Revenue Code inhibit the enforceability of the Plan's continuing obligation to retired * * * employees. If the Plan is unable to honor its obligation, liability for those benefits would have to be included in determining * * * liability to the PBGC [*5]

If the allocated assets of * * * separate plan are insufficient to satisfy all benefits guaranteed by the PBGC, disregarding those benefits that are being paid by the Plan; * * * is liable to the PBGC for the amount of the deficiency. Note that under Section 4062(b)(2) of the Act, that liability may be limited to 30 percent of your company's net worth shortly before the termination date. The PBGC has authority under Section 4067 of the Act to arrange extended terms for the payment of amounts owed to it under Section 4062(b).

To place participants' benefits in their proper priority category under Section 4044 of the Act, and to estimate the amount by which the assets of * * * separate plan may be insufficient to satisfy guaranteed benefits, you must determine which benefits are guaranteed. As all of the benefits under the Plan appear to be basic pension benefits, the amount that would be guaranteed depends on the termination date, as benefit increases are guaranteed at a rate of 20 percent or \$20 per month (whichever is greater), for each 12-month period prior to termination that the increase has been in effect. See Act § 4022(b)(8). The benefit increases that went into effect [*6] under the Plan on February 1, 1974 and February 1, 1975 would be subject to this phase-in rule. Other limitations on the PBGC's benefit guarantees are set forth in Section 4022(b) of the Act.

Questions 3, 4 and 5 in your letter ask how * * * potential liability can be estimated if its plan does not terminate until a later date, or if benefit levels are increased. Those calculations can be made using the principles discussed above. Subsequent benefit increases, including liberalization of the Plan's vesting provisions, would be guaranteed on a * * * phased-in basis.

I hope that this discussion is helpful. If you wish further assistance, please contact * * * of this Office, at the above address or by telephone at (202) 254-4868.

Henry Rose
General Counsel