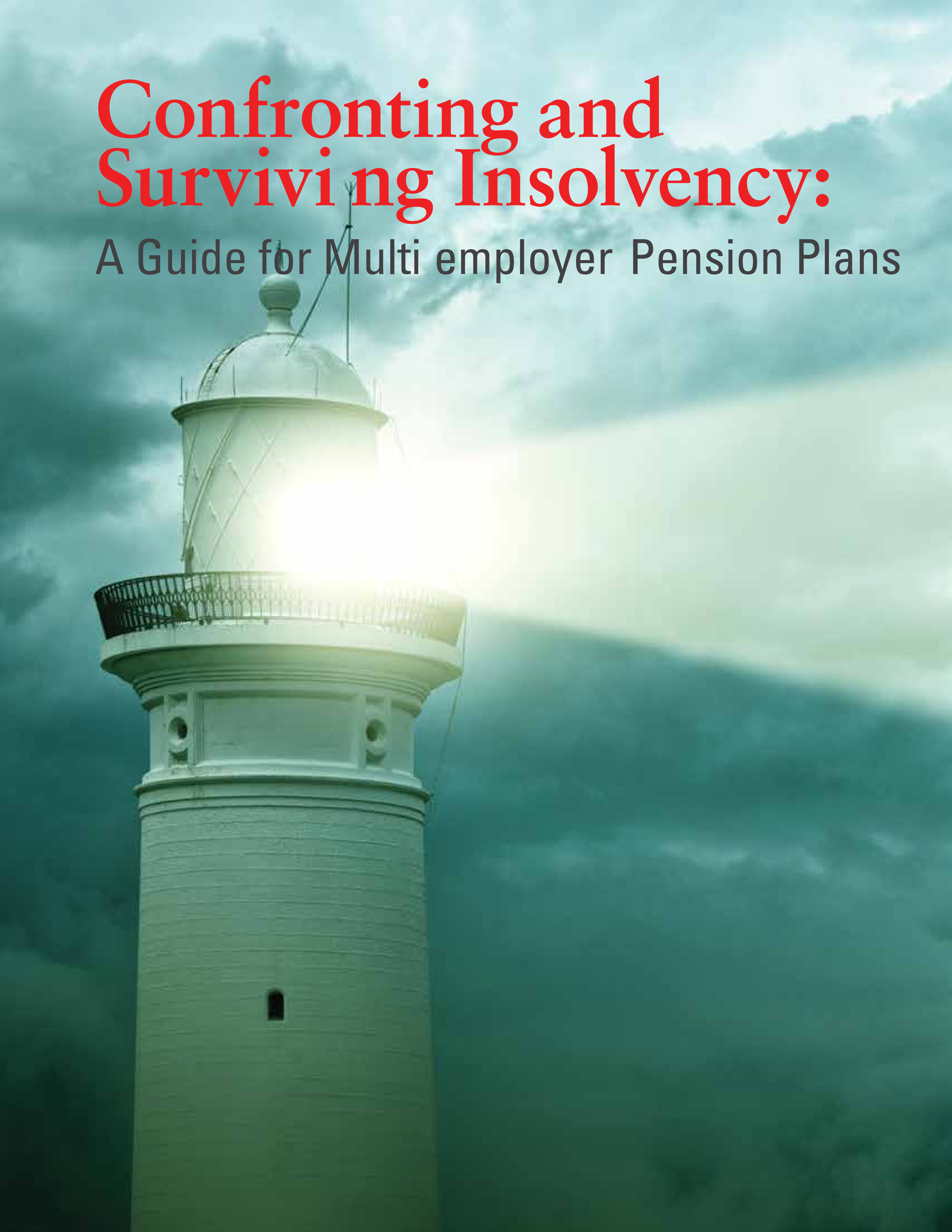
# Confronting and Surviving Insolvency:

## A Guide for Multiemployer Pension Plans



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What happens when a multiemployer pension plan seeks assistance from the Pension Benefit Guaranty Corporation? The author explains the insolvency process, including managing the plan after it begins receiving financial assistance.



From the Pension Protection Act of 2006 to the Multiemployer Pension Reform Act of 2014, Congress has passed a series of laws over the past decade designed to give pension plans greater tools to monitor their own financial health and to prevent insolvency.

Despite the greater variety of tools available, there are times when a pension plan simply cannot increase its assets or reduce its liabilities enough to avoid insolvency. Needless to say, there are significant issues still being addressed with respect to benefit suspensions, partitions and other tools that may be used to avoid insolvency. However, this article explains the process of managing plan insolvency; the steps pension plans, their trustees and their professional advisors must take to apply for financial assistance from the Pension Benefit Guaranty Corporation (PBGC);[1] and how to manage the plan going forward.

In 2016, PBGC paid $113 million in financial assistance to 65 insolvent multiemployer plans.[2] And, over the next decade, PBGC and most experts expect the number of plans, as well as the number of covered participants, to increase.

Therefore, it is important for plan sponsors and plan professionals to understand how insolvency works so they can be prepared to navigate the process.

## How Does a Pension Plan Become Insolvent?

Simply put, pension plan insolvency occurs when a pension plan no longer has assets sufficient to make benefit payments and to cover administrative expenses. Under ERISA, a multiemployer pension plan is insolvent "if the plan's available resources are not sufficient to pay benefits under the plan when due for the plan year."[3] As a practical matter, pension plan trustees and professionals will likely be aware of and carefully monitoring a plan's decreasing asset level for months or even years before the plan finally reaches insolvency.

And it is worth noting that the asset decrease may not always follow a straight-line trajectory. For example, a plan may be forecast to be able to pay benefits for ten months but then have a strong investment return that pushes the time horizon out to 15 months. Conversely, a plan that has 20 months before it is predicted to become insolvent might have a negative investment return and see that time frame reduced to 16 months. It is important for plan sponsors and plan professionals to carefully monitor asset levels to stay current on the ability of the fund to make benefit payments and cover expenses.

Moreover, at this time, it is equally important for plan sponsors to engage with their professionals, especially investment advisors, who can make recommendations on asset allocations during the winding-down process. Many investment advisors will recommend keeping asset allocation diversified as long as possible to maximize returns and to prevent any catastrophic investment losses as the asset levels decrease. At some point, most plans will move their remaining assets to relatively liquid investments, if not cash, in order to minimize any asset fluctuations during the last months before insolvency.

In addition, as it becomes apparent that a pension plan is likely to become insolvent in the upcoming plan year, the plan, generally through its actuary and/or attorneys, should reach out to PBGC for guidance on how to proceed with the upcoming insolvency. For larger plans, the agency may likely already be aware of the upcoming insolvency and may contact the plan first. In any event, PBGC professionals can offer valuable assistance to plan professionals and administrators in providing the required insolvency notices as well as preparing to apply for and to receive PBGC financial assistance.

## When Do Plan Sponsors Decide a Plan Is Insolvent?

Prior to the beginning of a new plan year, plan sponsors and plan professionals will examine the asset level and expected expenses of the plan. When it is evident that the assets on hand are not sufficient to pay expenses, the plan sponsor, which is the board of trustees of a multiemployer plan, should make a determination that the plan is going to become insolvent during the plan year and should authorize the plan professionals to take all required actions to comply with the legal and regulatory requirements for insolvent plans.

This discussion is not one that is taken lightly, and determining that the plan is going to be insolvent can be a difficult decision to make. Certainly, part of the discussion has to include an examination of the steps the plan has or could take to reduce benefits pursuant to a rehabilitation plan. And, with the passage of the Multiemployer Pension Reform Act (MPRA), a further discussion of benefit suspensions for pensioners in pay status and possible partition is also warranted. For some plans, these steps may be enough to avoid insolvency. However, at present, the standard for qualifying for partition or benefit suspensions under MPRA is quite high, and the cost of filing an application, especially in terms of professional fees, is significant. As a result, it appears that few plans will be able to use the newer MPRA mechanisms to avoid insolvency.

## What Notices and Forms Must Be Filed When a Plan Is Projected to Become Insolvent?

ERISA and the corresponding PBGC regulations set forth the requirements for notices a pension plan must send to interested parties regarding an impending insolvency.[4] First, the plan must send a formal notice of insolvency to PBGC, generally no later than 30 days after the plan sponsor determines that the plan is or may be unable to pay benefits for a plan year. The notice requires basic plan data, such as the plan name and Employer Identification Number, as well as more detailed data about the asset level of the plan, estimated amount of guaranteed benefits, estimated available plan resources and the most recent actuarial valuation.

In addition, the plan must send a notice of insolvency to all *interested parties*—that is, participants, beneficiaries, employee organizations representing participants and contributing employers. In general, the notice to interested parties regarding insolvency should also be issued within 30 days of the plan sponsor's determination that insolvency will occur. However, the notice to participants and beneficiaries in pay status may be enclosed with the first benefit payment made after the determination of insolvency, even if it causes the notice to be delivered after the 30-day period has expired. The notice to participants should include:

- The name of the plan
- A statement regarding the plan year in which the plan is or may become insolvent
- A statement of the plan's annual benefit payment and its available resources
- A statement explaining that benefits that exceed the greater of (a) the level that can be paid from the plan's resources or (b) the PBGC-guaranteed benefit will be suspended
- Name, address, telephone number and e-mail address of the plan administrator or other contact person to answer inquiries regarding benefits.

Within 60 days of the first day of a plan year in which the plan is expected to be or become insolvent, the plan also must send a notice of insolvency benefit level to interested parties and to PBGC. If the insolvency determination is made less than 120 days prior to the beginning of the plan year in which the plan will become insolvent, the notice of insolvency benefit level may be provided within 60 days after the insolvency determination.

The notice of insolvency benefit level provided to PBGC must contain largely the same information required for the notice of insolvency, to the extent that the information was not already provided. The notice of insolvency benefit level to participants (other than participants in or about to enter pay status) should include the plan name, the plan year for which the notice is being sent, the estimated amount of annual benefit payments under the plan, the estimated amount of the plan's available resources for the insolvency year and the amount of financial assistance, if any, requested from PBGC.

For participants and beneficiaries in or about to enter pay status, the notice of insolvency benefit level must include the name of the plan, the insolvency plan year, the expected monthly benefit to be paid to that participant or beneficiary, a statement that the benefit amount listed may be increased or decreased (but not below the PBGC-guaranteed level) and that a second notice will be sent before any such increase or decrease, an explanation of the PBGC-guaranteed benefit level and the contact information for the plan administrator or other individual who can handle inquiries about benefits.

It is worth noting that calculating the benefit amounts for the notice of benefit level to participants and beneficiaries in or reasonably expected to be in pay status can be a significant undertaking, especially for large plans. Given the volume of calculations that may need to be completed, it is worthwhile to begin this process as early as possible. In addition, plan sponsors and plan professionals should work closely with their assigned PBGC contacts to make sure that the estimated benefit calculations have been reviewed and approved by PBGC before the notices are sent, so that they do not need to be corrected later.

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Lawrence R. Beebe. International Foundation. 2017.

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## When and by How Much Will Benefits Be Reduced?

This is the most pressing question on the minds of participants, beneficiaries and trustees, as well as their sponsoring unions and employers. As a general matter, once the plan no longer has sufficient resources to pay benefits as set forth in the plan documents, the next phase is to pay benefits at the *resource benefit* level, which is the highest level of benefits that can be paid with available plan resources but no less than the PBGC-guaranteed amount (unless benefits under the plan are lower than the PBGC-guaranteed amount). While some plans may be able to pay benefits in excess of the PBGC-guaranteed benefit level for some time before the plan runs out of assets, others may simply move directly from the benefit levels in the plan documents to the PBGC benefit level.

The PBGC-guaranteed benefit is a monthly amount equal to 100% of the first $11 of the monthly benefit rate, plus 75% of the next $33 of the monthly benefit rate times the number of years of service. For example, let's assume a participant has an accrual rate of $60 per year of service. The guaranteed PBGC amount would be $11 + (75% of $33), which is equal to $35.75 per year of service—a reduction from the prior plan rate of $60. However, for participants whose monthly benefit rate is less than $11, there is no change in their benefits once the PBGC limits are applied. On the other hand, participants with higher plan benefit levels will experience greater benefit reductions than those with more modest benefit levels.

The PBGC guaranty generally applies to *basic benefits*—that is, the benefit amount payable at normal retirement age, many early retirement benefits (but not in excess of the amount payable at normal retirement age), survivor benefits and most disability benefits. However, any benefit improvements made within five years of insolvency are not included in the guaranteed benefit level.

The benefit reductions take place when the plan no longer has assets sufficient to pay the full benefits under the plan. If the plan has enough assets to pay less than the full benefits under the plan and more than the PBGC benefit level, it may do so until it runs out of assets. At that point, the plan will receive financial assistance and will have to reduce all benefits in excess of the PBGC-guaranteed benefit level to the PBGC benefit level.

## What Is the Process for Obtaining Financial Assistance From PBGC?

When a pension plan has insufficient assets to pay benefits, it may apply to PBGC for "financial assistance." Technically, PBGC financial assistance to a plan is a loan—In the event that the plan should have assets in the future, it is actually required to repay the loan. Most multiemployer plans that receive financial assistance from PBGC, however, do not find themselves in the position to repay the loan.[5]

The first step in seeking financial assistance from PBGC is submitting an application. Generally, the application is due 60 days before the beginning of the insolvency plan year but at least four months before insolvency, regardless of the 60-day rule. The application requires a significant amount of preparation—both in collecting data and documents for PBGC review and in preparing budget and actuarial projections in support of the application.

PBGC usually provides the plan with a list of requests for data that typically include bank registers, participant data, benefit payment lists, annual reports, investment account reports, audited financial statements and vendor contracts, as well as various studies of participant data and expected benefit payouts. After this information is compiled and sent to PBGC, the agency performs an audit of the plan, in which it reviews benefit payments made, contributions and withdrawal liability collection efforts, service provider contracts and similar documents.

Frequently, PBGC and its auditors have followup questions for the plan, and the audit process sometimes continues even after the financial assistance has commenced.[6] The length of the audit process will depend on a number of factors including, but not limited to, the size of the plan, the availability of plan records and the availability of auditors and plan staff to perform the required tasks. Needless to say, having well-organized, complete records is very helpful in expediting the audit process.

As the plan's resources decrease, it is important to keep PBGC informed of when financial assistance will be needed. When it becomes clear that the plan will not be able to pay benefits when due for a given month, the plan should inform PBGC of when that month is likely to occur and, to the extent it has not already done so, send the notice of insolvency benefit level. The plan administrator also will have to work with PBGC to provide a bank account to which PBGC will send the financial assistance payments, starting with the month prior to the month in which the plan is first unable to pay benefits from its existing assets. From then on, the plan will continue to receive PBGC financial assistance payments as long as it needs them.

## What Ongoing Obligations Do Plan Sponsors Have for an Insolvent Plan?

Once the plan begins receiving financial assistance, it will largely operate as it had before. The main difference is that benefits are paid from the PBGC financial assistance funds and, if applicable, benefits have been reduced to the PBGC-

## takeaways

- Pension plan insolvency occurs when a pension plan no longer has assets sufficient to make benefit payments and to cover administrative expenses.
- Pension plan trustees and professionals typically are aware of and monitoring a plan's decreasing asset level for months or years before the plan reaches insolvency. Plans should contact the Pension Benefit Guaranty Corporation (PBGC) for guidance once it becomes clear that a plan will become insolvent during the upcoming plan year.
- Notices that must be sent for an pending insolvency include a formal notice of insolvency to PBGC and a notice of insolvency to all interested parties—participants, beneficiaries, employee organizations representing participants, and contributing employers.
- When a pension plan has insufficient assets to pay benefits, it may apply to PBGC for financial assistance. The application is due 60 days before the beginning of the insolvency plan year but at least four months before insolvency.
- After plans begin receiving assistance from PGBC, they must continue to conduct activities such as collecting contributions and withdrawal liability and processing benefit applications and qualified domestic relations orders.

guaranteed benefit level. This means that the plan still must have trustees and administrative staff, hold regular trustees' meetings, collect contributions and withdrawal liability and process benefit applications and qualified domestic relations orders.

Clearly, as plan assets are dissipated, some services may no longer be needed, such as investment management and custodial services. However, because insolvent plans that continue to pay benefits and collect contributions are continuing plans, they still need to file annual reports, produce audited financial statements and actuarial valuations,[7] and distribute plan notices, such as annual funding notices, as they had before. And, to the extent there are changes in plan benefit levels throughout the insolvency period, updated insolvency benefit level notices must be sent to participants, as well as new notices for participants and beneficiaries who come into pay status after the initial notice of benefit insolvency level was sent. Throughout this process, the plan administrator should be in contact with PBGC to advise the agency of any changes in the plan's available assets or benefit obligations.

## What Can Plans Do to Prepare for Insolvency?

It is understandably difficult for plan sponsors to approach the task of addressing insolvency. After all, plan sponsors and their professional advisors work to ensure that their plans will be able to pay benefits. But, in some cases, plan demographics, poor investment returns or changes in an industry may simply make it impossible for a plan to continue to have enough assets to pay benefits. The good news is that the PBGC financial assistance program has been and hopefully will continue to be a valuable protection for plan participants.

Preparing for insolvency is a daunting task. First, plan sponsors must determine that there are no other avenues for the plan to pursue to continue operating. Once that determination has been made, plan sponsors should contact PBGC as early as possible to start the process of gathering the information necessary for the application for financial assistance.

At the same time, plan professionals should start working on the projections and benefit calculations required for the notices to be sent to PBGC and interested parties. As the plan assets decrease, plan administrators and financial advisors should monitor investment risk and return as well as asset levels so that they can keep PBGC informed of when financial assistance will be needed.

Finally, and most importantly, the plan must communicate effectively with its participants and beneficiaries and with the labor organizations and contributing employers about the changes that are expected. While insolvency is not easy to confront, with good preparation and communication, plan sponsors will find that they can continue to serve their participants and beneficiaries just as they had before.

## Endnotes

1. While it will not be addressed in this article, the financial situation of the Pension Benefit Guaranty Corporation (PBGC) has become increasingly precarious in recent years. At present, the PBGC multiemployer insurance program is predicted to exhaust its assets in 2025, and it could be "considerably sooner" if certain systemically significant pension plans become insolvent earlier. Press release, PBGC, "PBGC Reports—Multiemployer Program Needs Substantial Premium Increases; Single-Employer Program Likely to Eliminate Deficit by 2025" (June 17, 2016), available at www.pbgc.gov/news/press/releases/pr16-09>.
2. PBGC, Annual Report 2016, *Keeping Our Commitment to America's Workers*, at 2 (2016), available at www.pbgc.gov/Documents/2016-Annual-Report.pdf.
3. 29 USC §1426(b)(1).
4. For detailed information on the notices that must be sent, see 29 CFR §§4245.1-4245.8 (2017).
5. PBGC has noted that, initially, the statute anticipated that insolvency would be temporary, but the reality has been that most plans that reach insolvency do not become solvent again in the future.
6. PBGC is authorized to provide financial assistance to plans even while the application for financial assistance is still being processed. 29 USC §1431(c).
7. Current PBGC regulations do permit insolvent plans with less than $25 in nonforfeitable benefits to perform actuarial valuations once in three years.

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