



Defined Benefit Plan Terminations

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ASPPA COLLEGE OF PENSION ACTUARIES

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Agenda

- Types of Plan Terminations
- Benefit Liabilities
- Plan Sufficiency
- Plan Termination Steps
- PBGC Audits
- Problems
- Excess Assets

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Voluntary or Involuntary

- Plan terminations can be **voluntary** or **involuntary**
- An **involuntary termination** is generally accomplished by court action initiated by the PBGC
 - Generally, it will occur when PBGC anticipates that the employer's liability to PBGC for unfunded benefits is expected to increase unreasonably if the plan is not terminated
- A **voluntary termination** can be either a standard termination or a distress termination

Standard vs. Distress Termination

- A **standard termination** may occur when the terminating plan has assets sufficient to cover all benefit liabilities
 - PBGC Reg. 4041.21(a)(4)
 - i.e. no “unfunded benefit liabilities”
 - Benefit liabilities are defined in ERISA 4001(a)(16) and PBGC Reg. 4001.2 as “... the benefits of participants and their beneficiaries under the plan (within the meaning of section 401(a)(2) of the Code).”
- A **distress termination** is any other voluntary termination that is not a standard termination
 - Must meet one of 4 requirements by the PBGC
- Our focus today is on standard terminations

Standard Termination

- ERISA 4041(b)
- A plan may terminate in a standard termination only if
 - Plan assets are sufficient to satisfy all plan benefits, and
 - Plan Administrator follows prescribed steps

Reasons to Terminate

- IRS Form 5310 provides the following reasons for plan termination:
 - Change in ownership by merger
 - Liquidation or dissolution of employer
 - Change in ownership by sale of transfer
 - Adverse business conditions
 - Adoption of new plan
 - Other

Reasons to Terminate

- IRS indicates other acceptable reasons:
 - Substantial change in stock ownership
 - Employee dissatisfaction with the plan
 - Bankruptcy of employer

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Reasons to Terminate

- But we all know other reasons:
 - Contributions too costly
 - Fees too costly
 - Owner(s) ready to retire
 - Owner(s) hit 415 limit

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Considerations

- Is the plan sufficient or will the employer make a commitment to make it sufficient? (more later)
- What will replace the plan and how much will it cost?
- Will there be excess assets in the plan after termination?
- Is there a collective bargaining agreement that would bar termination?

Benefit Liabilities

- PBGC Reg. 4041.8(a)
- Benefits are determined under the plan's provisions in effect on the plan's termination date
- Notwithstanding the above, post-termination plan amendments will be taken into account if it doesn't decrease the value of plan benefits as of the termination date
- See Blue Book 2007-9 for further guidance

Benefit Liabilities

- Benefit liabilities are basically the sum of:
 - Lump sums to be paid - using greater of 417(e) factors or plan factors, as limited by 415 (if any)
 - Cost of annuities purchased (if any)
 - Amount transferred to the PBGC for missing participants (if any)

Benefit Liabilities

- IRC 411(b)(5)(B)(vi); Treas. Reg. 1.411(b)(5)-1(e)(2)
- For cash balance plans that use variable rates, must use
 - 5-year average of interest crediting rates; and
 - 5-year average of annuity conversion interest rates

Benefit Liabilities

- Blue Book 2009-10
- **Q.** How do the PPA 2006 changes in the interest rate and mortality table used in calculating minimum lump sum amounts apply in standard terminations where lump sums are paid in a year subsequent to the year of termination?
- **A.** Guidance on this issue was provided in Technical Updates 07-3 and 08-4. In summary:

Benefit Liabilities

- Blue Book 2009-10 (continued)
 - Technical Update 07-3 addresses the situation where the plan's termination date is before the PPA 2006 effective date of the changes to IRC 417(e) (i.e., plan years beginning after 2007). In these cases, the PPA 2006 changes do not apply. Minimum lump sums are determined based on the pre-PPA 2006 statutory requirements regardless of when the lump sum is paid.
 - Technical Update 08-4 addresses the situation where the plan's termination date is on or after the PPA 2006 effective date of the changes to IRC 417(e). In these cases, assuming the plan was amended to reflect the PPA 2006 changes before termination, the interest rate phase-in percentage and mortality assumption are tied to the annuity starting date, not the year of termination.

Benefit Liabilities

- Blue Book 2009-10 (continued)
 - For example, assume a calendar year plan is amended in 2008 to reflect PPA 2006 minimum lump sum assumptions and terminates on July 1, 2009. Also assume that the plan has a one-year stability period and a two-month lookback. Therefore, a lump sum paid in 2010 is calculated using the following assumptions:
 - Interest - based on the phase-in percentage for the plan year beginning in 2010 and the November 2009 rates. Accordingly, a lump sum paid in 2010 would be determined using a blended rate based on a 60 percent weighting of the November 2009 segment rates and a 40 percent weighting of the November 2009 30-year Treasury rate.
 - Mortality - based on the RP-2000 unisex mortality table project, in accordance with IRS rules, for annuity starting dates in 2010.

Benefit Liabilities

- 1.417(e)-1(d)(1)
- The present value under IRC 417(e)(3) must be valued using the same method as is used under the plan's actuarial equivalence. It is not clear under PPA, which changed the applicable mortality table beginning in 2008, whether this regulation still applies
 - Under the regulation, if the plan does not use pre-retirement mortality to determine the lump sum, then the IRC 417(e)(3) lump sum would also be valued without the use of pre-retirement mortality
 - There has been some comment with regard to the changes under PPA such that it may be a requirement to use pre-retirement mortality for the IRC 417(e)(3) lump sum regardless of the plan definition → *In my experience*, PBGC thinks this is correct

Benefit Liabilities

- Gray Book 2006-33 (paraphrased)
- A defined benefit plan provides lump sum benefits for employees eligible for early retirement, as the larger of:
 - (i) The present value of the immediate annuity using the plan's actuarial equivalence – the applicable mortality table and 7%; and
 - (ii) The present value of the participant's deferred annuity commencing at normal retirement age using the 417(e)(3) rates.
- Does this plan meet the minimum lump sum requirements of ERISA and the Internal Revenue Code?

Benefit Liabilities

- Gray Book 2006-33 (continued)
- No. Under regulation 1.417(e)-1(d)(1), the applicable interest rate and mortality table must be used to determine the minimum value of any benefit that is valued. Thus, a third value would need to be considered in this scenario – the present value of the early retirement benefit using the applicable interest rate and applicable mortality table.

Benefit Liabilities

- Gray Book 2006-33 (continued)
- The IRS is correct. The specific case does require a third calculation under 1.417(e)-1(d)(1) and 1.411(a)-11(a)(2)
- The key is that the lump sum at ERD is based upon the annuity commencing immediately
- Most plans are not drafted this way **deliberately**
- Moral: Read the document!

Benefit Liabilities

- Rev. Rul. 85-6
- Subsidized early retirement benefit in a terminated plan must be protected, even if conditions for the subsidy are not satisfied until some date after the plan termination
- Recommended ways of providing:
 - Purchase annuity contracts that would provide the subsidy, if the employee later meets the conditions; or
 - Provide the subsidized benefit whether or not the employee satisfies the conditions

Benefit Liabilities

- Treas. Reg. 1.411(d)-4 Q&A-2(a)(2)
- A participant is treated as receiving his entire vested benefit, if the payment is at least actuarially equivalent to his vested normal retirement age, even if a more valuable option could be elected
- The more valuable option must be available, regardless of whether the more valuable option is available immediately or upon future completion of eligibility requirements

Benefit Liabilities

- ASPPA ASAP 14-17
- In post-distribution audits of standard terminations, the PBGC has required a pre-retirement mortality adjustment for late retirement benefits, unless:
 - The plan has no pre-retirement mortality assumption; or
 - The plan specifically states that pre-retirement mortality does not apply to the late retirement benefit calculation

Benefit Liabilities

- 1.415(b)-1(c)(3)(i)
- “For a benefit paid in a form to which section 417(e)(3) applies, the actuarially equivalent straight life annuity benefit is the greatest of:
 - **(A)** The annual amount of the straight life annuity ... that has the same actuarial present value *as the particular form of benefit payable* [emphasis added], computed using the interest rate and mortality table, ..., specified in the plan for actuarial equivalence;
 - **(B)** The annual amount of the straight life annuity ... that has the same actuarial present value as the particular form of benefit payable, computed using a 5.5 percent interest assumption and the applicable mortality table ...; or
 - **(C)** [Ignored, since doesn't apply to small plans].”

Benefit Liabilities

- Example
 - Owner is retiring at age 65 in 2014
 - We want to pay him the maximum lump sum possible
 - Actuarial equivalence is 7% interest, UP-84 mortality
 - What is his maximum lump sum payable?

Benefit Liabilities

- Example (continued)
- What is the actuarial present value of the lump sum using the assumptions specified in the plan?
 - Amount calculated using 7% interest, UP-84 mortality; or
 - LS 7%, UP-84 = $\$17,500 * 104.82970 = \$1,834,520$
 - LS 5.5%, 2014 AMT = $\$17,500 * 139.49229 = \$2,441,115$
 - Maximum lump sum = $\text{Min}(\$1,834,520, \$2,441,115) = \$1,834,520$
 - Amount calculated using the greater of 7% interest, UP-84 mortality and 5.5% interest, 2014 applicable mortality table?
 - LS using 1.25%/4.57%/5.60%, 2014 AMT = $\$17,500 * 152.254232 = \$2,664,449$
 - Maximum lump sum = $\text{Min}(\text{Max}(\$1,834,520, \$2,664,449), \$2,441,115) = \$2,441,115$
- Moral: Amend the plan's definition of actuarial equivalence

Plan Sufficiency

- Plan sufficiency can be achieved differently for PBGC-covered terminations than terminations of plans not covered by Title IV of ERISA

Plan Sufficiency

Non-PBGC Plans

- Plan sponsor makes additional contribution(s)
- Reduce benefits on a pro-rata basis

PBGC Plans

- Plan sponsor makes additional contribution(s)
- Majority owner(s) elect to forgo benefits

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Plan Sufficiency

- Plan sponsor makes additional contribution(s) to satisfy all benefit liabilities
 - Commitment to fund the plan must be made in writing by the contributing sponsor and/or controlled group members
 - Deduction rules
 - Non-PBGC: Subject to IRC 404 rules
 - PBGC: IRC 404(o)(5) permits Title IV plans to contribute and deduct the difference between benefit liabilities and assets in the year of plan termination
 - If the sponsor or any controlled group member is in bankruptcy, the commitment must either be:
 - Approved by the bankruptcy court; or
 - Unconditionally guaranteed by a person not in bankruptcy

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Plan Sufficiency

- Reduce benefits on a pro-rata basis
 - Revenue Ruling 80-229 provides guidance
 - Not available for plans integrated with Social Security or that use permitted disparity
 - While an argument can be made that the NHCE can have their benefits reduced on a greater basis than HCE as long as IRC §401(a)(4) nondiscrimination rules are satisfied, I think that is a **bad** idea

Majority Owner

- PBGC Reg. 4041.2
- Owns, directly or indirectly, 50% or more of:
 - An unincorporated trade or business;
 - The capital or profits in a partnership; or
 - The voting stock or value of all stock of a corporation

Majority Owner

- Attribution rules of IRC 414(b) and 414(c) – and therefore IRC 1563(e) – apply
- Options qualify as ownership
- No lookback as in substantial owner definition!
- Family attribution rules of IRC 1563(e)
 - Spouse to spouse
 - Parent to minor children (under 21)
 - Minor child to parents
 - If ownership > 50%, from grandparents, parents, children, and grandchildren
 - E.g. An underfunded plan with 100% owner son, son's wife, and son's mother cannot terminate in a standard termination without fully paying out mom
- See Blue Book 2011-8 for further guidance

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Majority Owner

- Blue Book 2004-6
- **Q.** A plan is terminating in a standard termination. A husband and wife are both participants in the plan and each owns 40 percent of the contributing sponsor. Is each a majority owner and thus able to elect alternative treatment of his or her benefit in accordance with 29 CFR 4041.21(b)(2)?
- **A.** Yes. Under the constructive ownership rules of Code sections 414(b), each spouse would be a majority owner and thus able to elect an alternative treatment of his or her benefit in accordance with 29 CFR 4041.21(b)(2). See Code section 1563(e)(5) and Treas. Reg. 1-414(b)-1.

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Majority Owner

- Blue Book 2004-6 (continued)
- **Q.** Three persons are each participants in the plan and each owns one third of the stock of the contributing sponsor and each has an unrestricted option to buy out the other owners (subject to an ordering rule). Is each of these persons a majority owner and therefore able to elect an alternative treatment of his or her benefit in accordance with 29 CFR 4041.21(b)(2)?
- **A.** Yes. If three persons (whether or not related) each owned one-third of the contributing sponsor, with each owner having an unrestricted option to buy out the other owners (subject to an ordering rule), each would be a majority owner under the constructive ownership rules of Code section 414(b) and thus able to elect an alternative treatment of his or her benefit in accordance with 29 CFR 4041.21(b)(2). See Code section 1563(e)(1) and Treas. Reg. 1.414(b)-1.

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Majority Owner

- Blue Book 2007-8
- **Q.** PBGC's standard termination regulations provide that a majority owner ... may elect to forgo receipt of his or her plan benefits to the extent necessary to enable the plan to satisfy all other plan benefits ... Assume that two or more participants are each substantial owners, but not majority owners, and together have a 50% or greater ownership interest. Assume further that they agree among themselves that they will each elect such an alternative treatment under the majority owner rules. May they elect the alternative treatment?
- **A.** To be eligible to elect an alternative treatment under the majority owner rules, a participant must be a majority owner (taking into account the constructive ownership rules). There is no aggregation of ownership interests among participants (except to the extent provided under the constructive ownership rules).

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Majority Owner “Waiver”

- PBGC Reg. 4041.21(b)(2)
- One or more “majority owners” may agree to forgo all or a portion of his or her benefit to extent necessary to satisfy all other benefit liabilities

Majority Owner “Waiver”

- “Waiver” is misnamed → call it something like “election to forgo benefits”
- The IRS does not recognize **waivers** for purposes of minimum funding requirements
- Thus a “waiver” made for the purpose of reducing benefit liabilities will not reduce minimum required contributions under IRC 412 and 430

Majority Owner “Waiver”

- The agreement must be in writing;
- The agreement must not be inconsistent with a qualified domestic relations order (QDRO);
- If the benefit is greater than \$5,000, the spouse, if any, must consent in writing; and
- **In my opinion**, the plan should be amended prior to the plan termination date to change the asset allocation method to correspond with the language of the waiver

Majority Owner “Waiver”

- Timing
 - Waiver must be made, and spouse must consent, during period
 - Beginning with date of issuance of notice of intent to terminate (NOIT) and
 - Ending with date of final distribution
 - Timing can be vital on stock sale of company
 - Must make sure NOIT is issued, and waiver is made, prior to date of closing of sale (i.e. must be a majority owner when sale is made → no lookback as in substantial owner definition)
 - See Blue Book 2004-5 for further guidance

Majority Owner “Waiver”

- If amount of waiver was incorrect and there are plan assets remaining after paying benefits to all other plan participants, the remaining assets must be distributed to the majority owner to satisfy his plan benefits
- See Blue Book 2005-6 for further guidance

Administration During Plan Term

- PBGC Reg. 4041.22 (and Standard Termination Filing instructions at II.B.)
- Plan Administrator may not distribute plan assets in connection with termination until PBGC’s review period ends (except as described next)
- Plan Administrator must continue to carry out normal plan operations during termination process, including:
 - Putting participants into pay status
 - Collecting contributions
 - Investing plan assets

Administration During Plan Term

- However, during the period beginning with the issuance of the NOIT until PBGC's review period ends, the Plan Administrator may not: (except as described next)
 - Purchase irrevocable commitments (annuity contracts) to provide any plan benefits
 - Pay any plan benefits attributable to employer contributions (other than death benefits) *in any form other than as an annuity*

Administration During Plan Term

- Exception: Plan Administrator may provide benefits attributable to employer contributions in a form other than as an annuity if:
 - The participant terminated employment or is otherwise permitted to receive the distribution;
 - The distribution is consistent with prior practice; and
 - The distribution is not likely to jeopardize the plan's sufficiency for plan benefits

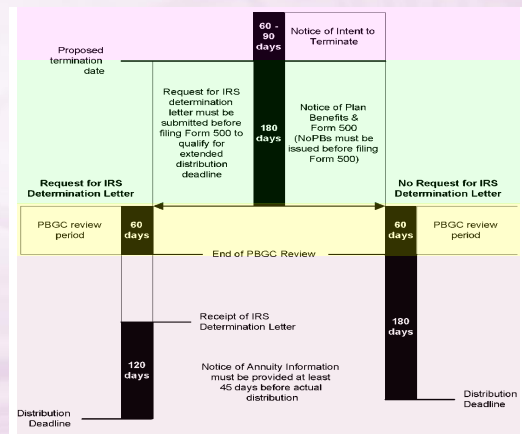
Plan Termination Steps

1. Resolution / Plan Amendment(s)
2. 204(h) Notice
3. Notice of Intent to Terminate (if PBGC-covered)
4. Notice to Interested Parties (if filing for FDL)
5. IRS Determination Letter Request (Forms 5310, 6088, 8717)
6. Notice of Plan Benefits
7. PBGC Standard Termination Notice (Form 500, Schedule REP-S, Schedule EA-S)
8. Notice of Annuity Information
9. Missing Participants / Distribution of Plan Assets
10. Notice of Annuity Contract
11. PBGC Post-Distribution Certification (Form 501, Schedule MP)
12. Final PBGC Premium Filing and IRS Form 5500 / 5500-SF / 5500-EZ

Plan Termination Steps

Step	Timing
Resolution / Plan Amendment(s)	Generally by date of plan termination (DOPT)
ERISA 204(h) Notice	At least 15 days (45 days if large plan) prior to freeze
Notice of Intent to Terminate	At least 60 days but no more than 90 days prior to proposed DOPT
Notice to Interested Parties	At least 7 days but no more than 21 days prior to filing Form 5310
IRS Form 5310, etc.	Prior to filing PBGC Form 500
Notice of Plan Benefits	Prior to filing PBGC Form 500
PBGC Form 500, etc.	No later than 180 days after DOPT
Notice of Annuity Information	At least 45 days prior to distribution of plan assets
Distribution of Plan Assets	Generally no more than 1 year after termination date (exceptions apply)
Notice of Annuity Contract	No later than 30 days after distributions are completed
PBGC Form 501, etc.	No later than 30 days after final distribution is made (no penalty if 90 days after distribution deadline)
Final PBGC premium filing	Regular filing date for the plan year in which final distribution occurs
Final Form 5500 / 5500-SF / 5500-EZ	No later than last day of 7th month after final distribution

Plan Termination Steps



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Resolution and Amendments

- Resolution for corporations
- Written Record of Action for sole proprietors and partnerships
- Only need to update if current plan doesn't already include

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Resolution/Amendment Content

- The date accruals will be suspended;
- The Date of Plan Termination (DOPT);
- That participants become fully vested;
- That no new entrants shall become eligible after the DOPT;
- That no new entrants shall become eligible after benefit accruals are suspended;
- Any changes to the 417(e) rules;

Resolution/Amendment Content

- The method of allocating excess assets or a deficiency of assets, or the percentage of excess assets which are to be transferred to a Qualified Replacement Plan;
- Any removal of benefits which are not protected by IRC 411(d)(6) but are considered to be benefits under IRC 401(a)(2) which must be paid before a reversion of assets to the employer; and
- Any changes to the plan document to bring the plan into compliance with law or regulation changes.

Timing of Amendments

- Remember that benefits are determined under the plan's provisions in effect on the plan's termination date, unless the amendment does not decrease the value of benefits
- Must be adopted prior to DOPT
 - Removal of benefits not protected by 411(d)(6)
 - Change in 417(e) rates for PPA '06
 - Change in method of allocating excess assets
- Should be adopted prior to DOPT
 - Asset allocation if plan is insufficient
 - Pro-rata reduction for non-PBGC plans
 - Majority Owner will be last in line for PBGC plans
 - Not needed for one man plans
 - Providing lump sum distributions if not available (e.g. to retirees)
 - All amendments, if not seeking a FDL
- May be adopted after DOPT if necessary to obtain a FDL
 - Amendments to bring the plan into compliance with laws or regulations

204(h) Notice

- ERISA 204(h), as amended by EGTRRA, requires that a notice must be provided if there is a reduction in future benefit accruals
- Applies to applicable pension plans that are subject to funding requirements of IRC 412
- Must be provided to all participants, beneficiaries, alternate payees, etc. whose future benefit accrual is expected to be reduced by an amendment

204(h) Notice

- Final regulations clarify:
 - ERISA 204(h) notice is not needed for plan amendments that substitute the 417(e)(3) segment rates for 30-year Treasury rates
 - Other notices may suffice for complying with the 204(h) requirements

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204(h) Notice

- Examples of other notices may suffice for complying with the 204(h) requirements
 - ERISA 101(j) notices that apply when IRC 436 restrictions on accruals, shutdown benefits and accelerated benefit payments
 - Notices required for multiemployer plans in reorganization, insolvency, or reducing plan benefits
 - Notices required for retroactive amendments under IRC 412(d)(2) [former 412(c)(8)]

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204(h) Notice Timing

- Plans with fewer than 100 participants have a 15-day notice period
- Larger plans have a 45-day notice period (exceptions on next slide)
- Multiemployer plans have a 15-day notice period

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204(h) Notice Timing

- Exceptions for larger plans:
 - The 15-day rule also would apply to a plan amendment adopted in connection with a corporate acquisition or disposition
 - A plan amendment in connection with a merger, transfer, or consolidation of assets or liabilities that significantly reduces an early retirement benefit or retirement-type subsidy but does not significantly reduce the rate of future benefit accrual has until 30 days after the effective date of the amendment

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204(h) Notice Content

- Must “provide sufficient information to enable a participant to understand the effect of the amendment”
- Content must permit the applicable individual to determine the approximate magnitude of the reduction available to the individual, which can be satisfied through illustrative examples

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204(h) Notice Content

- If participants have a choice between an old and a new benefit formula (like in a cash balance conversion), participants must be given sufficient information to choose between the two
- Individualized benefit statements may be used in lieu of illustrative examples if they include the same information

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Notice of Intent to Terminate

- Applies to PBGC-covered plans
- Issued to “affected parties” as of the proposed termination date
 - PBGC Reg. 4001.2
 - Includes participants, beneficiaries, alternate payees, and unions
 - Does not include the PBGC
- Provided 60-90 days prior to proposed termination date

NOIT Delivery

- Standard Termination Filing instructions at II.A.1.
- Delivery by any method reasonably expected to ensure receipt
 - Hand delivery
 - First class mail
 - Electronic delivery by electronic media
 - Commercial delivery service to affected party’s last known address (deemed issued on date of delivery or evidence of postmark)
- Posting is not a permissible method

NOIT Content

- Model Notice in PBGC's Standard Termination Filing instructions
- Identifying information
 - Name of plan and plan number
 - Name and EIN of each contributing sponsor
 - Name, address, and phone number of person to be contacted with questions

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NOIT Content

- Intent to terminate plan
 - A statement that the PA intends to terminate the plan in a standard termination as of a specified date and will notify affected parties if date changed or if termination does not occur
- Sufficiency requirement
 - A statement that to terminate in a standard termination plan assets must be sufficient to provide all benefits under the plan

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NOIT Content

- Cessation of accruals
 - As statement that:
 - Benefit accruals will cease as of termination date, but will continue if plan does not terminate
 - An amendment has been adopted ceasing benefit accruals as of proposed term date (or earlier specified date) whether or not terminated; or
 - Benefit accruals had ceased, in accordance with ERISA 204(h), as of date before NOIT issued
 - May require different NOITs for different participants
 - This satisfies the 204(h) notice requirement

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NOIT Content

- Annuity information
 - Either include contents of Notice of Annuity Information; or
 - Statement indicating that:
 - Annuity contracts may be purchased from an insurer that is yet to be identified; and
 - Affected parties will receive a supplemental notice identifying the insurer at least 45 days prior to distribution

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NOIT Content

- **Benefit information**
 - A statement that each affected party entitled to benefits will receive a written notification regarding his or her plan benefits (Notice of Plan Benefits)
- **Summary Plan Description**
 - A statement as to how an affected party can get the latest updated Summary Plan Description
- **Continuation of monthly benefits (for persons in pay status)**
 - A statement that their periodic benefits will not be affected by the plan's termination; or
 - An explanation of how their periodic benefits will be affected under the provisions of the plan

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NOIT Content

- **Extinguishment of guarantee**
 - A statement that after plan assets have been distributed in full satisfaction of all plan benefits with respect to a participant or a beneficiary, the PBGC no longer guarantees that participant's or beneficiary's benefits

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Notice to Interested Parties

- Informs participants of their rights regarding the plan termination
- Only required if requesting a FDL
- Not required for one man plans
- Provided 7-21 days prior to filing Form 5310
- Sample notice in Announcement 2013-15

Determination Letter Request

- Filed prior to filing PBGC Form 500
- Not required but can be helpful
- What does a FDL do?
 - It is “the opinion of the Service as to the qualification of the particular plan involving the provisions of §§401....”
 - It does not apply to taxability issues under §404
 - It covers document issues, not operational issues
 - See Revenue Procedure 2013-6, Section 21 (“What Effect Will An Employee Plan Determination Letter Have?”)



Determination Letter Request

- Pros
 - Provides protection from risk of disqualification
 - More protection from problems if the Plan were later to be chosen for examination
 - More protection both for the client and for the service provider
 - No reliance on Opinion Letter or Advisory Letter for plan termination
 - Extends the time for final distribution of benefits for PBGC-covered plans (Is this a good thing?)

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Determination Letter Request

- Cons
 - Does not establish validity of termination
 - Does not establish that benefit distributions were correct
 - Issues discovered by the reviewing agent are no longer allowed to be cleaned up without penalty
 - More likely to be chosen for an audit “to see if the distributions were made as proposed by the taxpayer”
 - IRS User Fee (\$2,000 for single employer plans and \$3,000 - \$15,000 for multiple employer plans (dependent on number of employees maintain the plan))

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Notice of Plan Benefits

- Send to each “affected party”
 - Not required to send to a participant whose benefits are paid out prior to NOPB due date → see Blue Book 2007-6
- Provided prior to filing PBGC Form 500
- Delivered in same manner as Notice of Intent to Terminate

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NOPB Content

- Identifying information
 - Name of plan and plan number
 - Name and EIN of each contributing sponsor
 - Name, address, and phone number of person to be contacted with questions
- Proposed termination date given in NOIT (and any extended proposed termination date)
- If benefit amount in notice is estimate, a statement stating so and that benefits paid may be greater than or less than estimate

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NOPB Content

- For persons not in pay status for more than a year as of proposed termination date
 - Personal data needed to calculate person's benefits, e.g., DOB, DOH, credited service, salary history (if applicable)
 - Statement requesting that affected party promptly correct any information he/she believes not correct
 - If any necessary data not available, the best available data, along with statement informing affected party of data not available and affording him or her opportunity to provide

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NOPB Content

- For persons in pay status as of proposed termination date
 - Amount and form of participant's or beneficiary's benefits payable as of proposed termination date
 - Amount and form of benefits, if any, payable upon participant's death and name of beneficiary
 - Amount and date of any increase or decrease in benefit that has occurred or is scheduled to occur after proposed termination date with explanation, and reference to pertinent plan provision

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NOPB Content

- For persons with valid elections (or de minimis benefits) as of proposed DOPT
 - Amount and form of participant's or beneficiary's benefits payable as of indicated projected date
 - Amount and form of benefits, if any, payable upon participant's death and name of beneficiary
 - Amount and date of any increase or decrease in benefit that has occurred or is scheduled to occur after proposed termination date with explanation, and reference to pertinent plan provision

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NOPB Content

- For persons with valid elections (or de minimis benefits) as of proposed DOPT (continued)
 - If benefits will be paid in any form other than lump sum, and the age at which, or form in which, the plan benefits will be paid differs from the normal retirement benefit, an indication of:
 - The age or form stated in the plan; and
 - The age or form adjustment factors

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NOPB Content

- For persons with valid elections (or de minimis benefits) as of proposed DOPT (continued)
 - If benefits will be paid in a lump sum
 - An explanation of when LS may be paid w/o consent
 - A description of the mortality table and interest rate(s) used and a reference to pertinent plan provisions
 - An explanation of how interest rates are used to calculate lump sums and a statement that the use of a higher interest rate results in a smaller LS
 - A statement that the applicable interest rate may change before distribution

NOPB Content

- For persons without valid elections as of proposed DOPT (i.e. most participants)
 - The amount and form of benefits payable at NRA in any one form permitted under the plan
 - Alternative benefit forms, including those payable to a beneficiary upon the person's death
 - If the person is entitled to a benefit payable before NRA, the amount and form of benefit that would be payable at the earliest commencement date (or, if more than one such form is payable at such date, any one of those forms) and whether the benefit on such date would be subject to future reduction

NOPB Content

- For persons without valid elections as of proposed DOPT (continued)
 - If benefits may be paid in a lump sum
 - A description of the mortality table and interest rate(s) used and a reference to pertinent plan provisions
 - An explanation of how interest rates are used to calculate lump sums and a statement that the use of a higher interest rate results in a smaller LS
 - A statement that the applicable interest rate may change before distribution

Standard Termination Notice

- PBGC Form 500
 - Standard Termination Notice / Single-Employer Plan Termination
 - With Schedule EA-S, Standard Termination / Certification of Sufficiency
 - With Schedule REP-S, Standard Termination / Designation of Representative

Standard Termination Notice

- Filed within 180 days after the proposed termination date
 - May be filed before DOPT
 - If in a hurry, issue NOIT, NOPBs, and STN at the same time
 - If filing for FDL, do so at the same time or prior to filing the STN
- See Blue Book 2006-4 if you fail to file timely

PBGC Schedule EA-S

- Certification of Actuary that assets are projected to be sufficient to provide all benefit liabilities as of proposed termination date
 - As required by ERISA 4041(b)(2)(A) and PBGC Reg. 4041.21(a)(4)
- Must be signed by plan's enrolled actuary
- Per Standard Termination Filing instructions at IV.B.:

PBGC Schedule EA-S

- Line 4 asks for proposed distribution date
- Note example in instructions
 - *The plan administrator files the Form 500 on March 24, 2008. The earliest possible proposed distribution date is May 24, 2008. The latest possible proposed distribution date is November 19, 2008*
 - This is not accurate of course as the measurement date is not the filing date but the receipt date as indicated below
 - Nevertheless it's what is commonly used

PBGC Schedule EA-S

- Line 6 asks for estimated FMV of plan assets available to pay benefits as of proposed distribution date
 - Subtract liabilities, including benefit liabilities expected to be paid before proposed distribution date (but not such liabilities expected to be paid at such date)
 - May include as an asset the value of a commitment to contribute additional sums needed to make the plan sufficient [per PBGC Reg. 4041.21(b)(1) discussed above]

PBGC Schedule EA-S

- Line 7 asks for estimated value of plan benefits as of proposed distribution date
 - Instructions offer nothing additional here
 - How to handle majority owner waivers?
 - Do you show as asset and liability?
 - i.e. show full amount of liability on line 7 and include on line 6 estimated amount of waiver
 - Or do you net out of liability on line 7 and show estimated asset amount on line 6
 - This is how I do it

PBGC Review Period

- PBGC Reg. 4041.26
- PBGC has 60 days after receipt to review a Form 500 filing for compliance
 - PBGC will notify filer in writing of receipt date so filer can determine when review period will expire
 - PBGC starts the 60-day period when they receive Form 500, not based on the postmark
- Review period may be extended if PBGC and PA agree, in writing, before expiration of review period
 - More than one extension may be made

PBGC Review Period

- PBGC will send one of three responses
 - Acknowledgment letter
 - Notice of incomplete filing
 - Notice of noncompliance (NON)

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PBGC Review Period

- PBGC may request additional information
- Information usually required to be submitted within 30 days of request
- Request for additional information suspends running of 60-day period
 - Begins running again on the date information is received
 - Continues for the greater of:
 - Number of days remaining in original period; or
 - Five business days from day information is received

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Notice of Annuity Information

- PBGC Reg. 4041.27
- Send to each plan participant no later than 45 days prior to distribution of plan assets
- As part of Notice of Intent to Terminate, the Plan Administrator must provide:
 - Identity of potential insurers
 - Names and addresses of insurers or potential insurers from whom annuity contracts may be purchased
 - DOL issued Interpretive Bulletin 95-1 regarding the selection of an insurer
 - Common practice is to list a handful of major insurers

Notice of Annuity Information

- Change in identity of insurers
 - A statement that, if contract purchased from insurer not identified, a supplemental notice will be provided at least 45 days before distribution identifying actual insurer
- Information on state guaranty associations
 - A statement to affected parties that:
 - The insurance company takes over responsibility for paying benefits upon purchase of annuity
 - All states, Washington DC and Puerto Rico have guaranty associations protecting policy holders in case of failure of insurance company
 - Such association is responsible for all, part, or none of annuity if insurer cannot pay
 - Each association has dollar limits on guaranty coverage with a general explanation of limits
 - Generally participant is covered based on state of residence at time of failure to pay, and
 - How to obtain guaranty information from PBGC

Notice of Annuity Information

- In lieu of the above annuity information, the Plan Administrator may instead elect to later distribute a supplemental notice of annuity information containing the above information
- In such case, the NOIT must include a statement indicating that:
 - Annuity contracts may be purchased from a yet-to-be-identified insurer to provide some or all benefits
 - Affected parties will receive a supplemental notice identifying the insurer at least 45 days prior to date of distribution

Notice of Annuity Information

- My practice is to provide an annuity notice with the NOIT
- It includes all of the information required above, as well as a list of major insurers (with names and addresses)
- If ultimate insurer not named, a supplemental notice would be issued

Notice of Annuity Information

- Blue Book 1998-11
- **Q.** How can the notice that identifies the insurer be provided 45 days before distribution when most insurers keep bids open only for a very short time?
- **A.** If the plan administrator knows who the insurer will be when this 45-day notice is issued, the notice must identify that insurer. However, if the plan administrator does not yet know for sure, the regulations provide that the notice may contain a list of those insurers the plan administrator is considering. Any list of insurers should be reasonable in number and include only those insurers from whom the plan administrator has solicited, or reasonably intends to solicit, actual bids.

Missing Participants

- Distribute benefits of missing participants by:
 - Purchasing annuities; or
 - Paying the value of the benefit to the PBGC
- Cannot roll over into an IRA



Missing Participants Program

- Currently only available for terminating single-employer defined benefit plans
- Proposed regulatory changes
 - Implement PPA expansion of program to:
 - DC plans
 - Multiemployer DB plans
 - Professional service employer plans (25 or fewer active participants)
 - Expanded program applicable to distributions made after final regulations are issued

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Missing Participants Program

- Step 1: Conduct diligent search
 - Inquiry of beneficiaries known to plan administrator as to whereabouts of participant
 - Use of commercial locator service
 - Cannot begin more than 6 months before NOIT is issued
- Step 2: Select a deemed distribution date (no later than distribution deadline)

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Missing Participants Program

- **Step 3: Calculate value of missing participants' benefit as of deemed distribution date**
 - Example: Designated Benefit is the greater of:
 - Lump sum payable under plan assumptions
 - Present value of most valuable benefit under missing participant annuity assumptions

Missing Participants Program

- **Step 4: Send completed Schedule MP and attachments with Post-Distribution Certification (Form 501) to PBGC**
 - Enrolled Actuary must sign Schedule MP
- **Step 5: Send payment and Missing Participant Payment Voucher to PBGC's Lockbox**

Missing Participants Program

- If a participant fails to sign and return a benefit election form, he is not a missing participant → see Blue Book 2002-11
- If a participant fails to sign and return a benefit election form, plan must buy an annuity that preserves all optional forms → see Blue Book 2004-7
- If a participant elects and annuity and plan is unable to find an insurer, he is not a missing participant → Blue Book 2002-12

Distribution of Plan Assets

- Distributions may begin after PBGC review period and must be distributed by later of:
 - 180 days after PBGC's review period; or
 - 120 days after receiving FDL
 - PBGC Reg. 4041.28(a)
- If neither apply, then when “administratively feasible”
 - A matter of facts and circumstances
 - Generally, a period of one year from the plan termination date is deemed to comply
 - Also there could also be circumstances in which it takes a long time to be able to sell a plan asset (e.g. real estate)

Distribution of Plan Assets

- PBGC Reg. 4041.28(c), 4041.28(d)
- Plan Administrator distributes assets by purchasing annuity contracts from an insurer to satisfy all benefit liabilities that must be so provided (and provides each participant with a copy of the contract; and/or
- By otherwise providing benefit liabilities that need not be provided in annuity form (i.e. pay out lump sums)

Distribution of Plan Assets

- AFTAP restrictions remain in effect post-termination; however, restrictions do not apply if the accelerated payment or purchase of an annuity is to carry out the termination of the plan

Notice of Annuity Contract

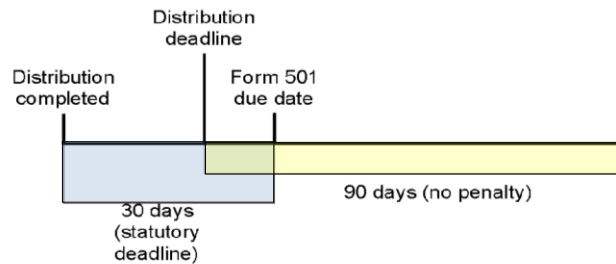
- Send to participants who will be receiving annuities
- Must be provided no later than 30 days after distributions are completed

PBGC Form 501

- PBGC 4041.29
- Filed within 30 days after final distribution is made
- No penalty assessed if filed within 90 days after distribution deadline
- PBGC will not nullify an otherwise valid standard termination if filing is late → see Blue Book 2010-15

PBGC Form 501

Standard Termination Timeline: Post-Distribution Certification



PBGC Audits

- PBGC will definitely audit:
 - All standard terminations of plans with more than 300 participant
 - Plans with an indication of a problem (complaints from participants or practitioners)
 - All plans that distribute assets before or without filing a Standard Termination Notice
- For plans with fewer than 300 participants, PBGC randomly selects plans to audit

PBGC Audits

- Focus of audit is whether or not participants got proper distributions (both benefits and optional forms)
- Audits are very comprehensive and may require
 - Plan documents from plan inception
 - Payroll records from date of hire

PBGC Audits

- Standard Termination Filing instructions at II.K.
- Must maintain all records necessary to demonstrate compliance with section 4041 of ERISA and 29 CFR Part 4041 for six years after the date the Form 501 is filed

PBGC Audits

- PBGC required corrective action in approximately
 - 16% of the cases for FY 2009 → see Blue Book 2010-12
 - 22% of the cases for FY 2010 → see Blue Book 2011-5

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PBGC Audits

- Blue Book 2010-12, Blue Book 2011-5
- Common errors
 - Not vesting terminated participant who had not incurred a five-year break in service and had not received a distribution of the entire benefit as of DOPY
 - Does the five-year break in service rule apply to defined benefit plans? Is there formal guidance? IRS' application of this rule in the field seems to be inconsistent.
 - Not protecting accrued benefits under prior plan provisions

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PBGC Audits

- Common errors (continued)
 - Not paying the top heavy benefit if greater than the accrued benefit
 - Using incorrect interest rate, mortality table, or participant age in calculating lump sums
 - Using assumptions adopted in post-termination amendments to calculate lump sums

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PBGC Audits

- Common errors (continued)
 - Missing participants' benefits not transferred to PBGC
 - Failing to obtain appropriate elections and spousal consents
 - Waiving benefits by non-majority owners
 - Failing to include all benefit options in annuity contracts

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PBGC Audits

- Common errors (continued)
 - Failing to send the total value of missing participants' benefits to the PBGC
 - Failing to use a 5-year average for cash balance interest crediting rates and annuity conversion rates (post-PPA)

Insufficient Assets

- PBGC Reg. 4041.28(b)
- If assets are found to be insufficient when distributions are to begin, the Plan Administrator should:
 - Not make any distribution of assets to effect the plan's termination; and
 - Promptly notify the PBGC
- See Blue Book 2005-8

Failure to Distribute

- If assets are not distributed within the required period without an extension, the termination is nullified
- All actions taken to effect the plan's termination are null and void, and the plan becomes an ongoing plan
- Plan Administrator must notify affected parties in writing that plan is not terminating or that the termination was invalid but that new NOIT being issued

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Failure to Distribute

- PBGC Reg. 4041.30, Standard Termination Filing instructions at II.J.
- Plan Administrator may request extension if reason is other than insufficiency
 - Consideration will be given to length of delay and whether ordinary business care and prudence was exercised in attempting to meet the deadline
 - If request filed later than 15th day before deadline, must include a justification for not filing request earlier
 - Example may be asset that is proving difficult to liquidate but that ultimately will be liquidated

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Failure to Provide Notices

- Form 500 instructions, Section II p.4
- If a plan administrator fails to provide any required information within the specified time limit, PBGC may assess a penalty of up to \$1,100 a day for each day that the failure continues. Under PBGC's penalty policy, the penalty rate is generally much lower — \$25 per day for the first 90 days and \$50 per day thereafter, with lower rates for small plans. PBGC may also pursue any other equitable or legal remedies available to it under the law, including, if appropriate, the issuance of a Notice of Noncompliance (NONC). *See 29 CFR § 4041.6 and PBGC's Statement of Policy on ERISA section 4071 penalties*, 60 Fed. Reg. 36,837 (July 18, 1995)
- <http://www.pbtc.gov/documents/071895.pdf>

Notice of Noncompliance

- PBGC will issue a NON whenever it makes one of the following determinations:
 - The plan administrator failed to properly issue the NOIT in accordance with its requirements
 - The plan administrator failed to properly issue NOPBs in accordance with its requirements
 - The STN, or any supplemental notice, was not filed in accordance with its requirements
 - As of the proposed distribution date, plan assets will not be sufficient to satisfy all benefit liabilities under the plan

Notice of Noncompliance

- Effect of Notice of Noncompliance
 - Ends the standard termination
 - Nullifies all actions taken to terminate plan
 - Renders the plan ongoing
- Plan Administrator may request reconsideration within 30 days after receipt of NON
 - PBGC Reg. 4003.32

Notice of Noncompliance

- PBGC Reg. 4041.30
- Upon PBGC's issuance of NON, affected parties must be notified in writing that:
 - Plan is not going to terminate; or
 - The termination was invalid but a new NOIT is being issued

Notice of Noncompliance

- Delivery of NON notice
 - Participants and beneficiaries who are employees or in pay status: by first class mail or hand delivery
 - Other participants and beneficiaries: any other manner reasonably calculated to reach them

Overfunded Plans

- Assets remaining after the satisfaction of all benefit obligations may revert to the company if the plan so provides
- The plan provision to allow reversion must have been in effect for at least five years (or since the inception of the plan, if less than five years)
 - Generally good practice to use this as the default provision when establishing the plan

Excise Tax on Excess Assets

- IRC 4980 imposes a 50% excise tax on reversions of excess plan assets
- The 50% tax is reduced to 20% if one of the following applies:
 - Employer establishes or maintains a qualified replacement plan (conditions apply);
 - Employer provides pro-rata benefit increases; or
 - Employer is in liquidation in bankruptcy

Qualified Replacement Plan

- At least 95% of the active participants in the terminated plan who remain as employees are active participants; and
- A direct transfer of 25% (or more) of the surplus of the original plan is made to the qualified replacement plan;



Qualified Replacement Plan

- The funds are allocated under the plan to the accounts of the participants
 - In the plan year in which the transfer occurs; or
 - Credited to a suspense account and allocated to the accounts of the participants no less rapidly than ratably over 7 years beginning with the year of the transfer

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Pro-Rata Benefit Increases

- 20% (or more) of the surplus assets are allocated to participants to provide pro-rata benefit increases in proportion to present value of accrued benefits
- Any benefit increase must meet the nondiscrimination requirements of IRC 410(b) and 401(a)(4)...if you want a tax qualified plan

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Pro-Rata Benefit Increases

- A benefit increase that does not meet these requirements will not result in a decrease in the excise tax rate from 50% to 20% but will reduce the amount of the reversion to which the excise tax rate is applied
- Any benefit increase that eliminates a reversion entirely, will eliminate the excise tax

Pro-Rata Benefit Increases

- If a participant cannot receive his share due to 415 it is OK to give the rest to others

Exceptions to the Excise Tax

- The reversion is transferred to an ESOP that meets certain conditions;
- Reversions to employers which have at all times been exempt from federal income tax; or
- Governmental plans within the meaning of IRC 414(d)

Techniques to Reduce Reversion

- Consider hiring family members of the owner and so they become participants in the plan
 - Watch out for 401(a)(4) issues
 - Make sure they are real employees
- If needed, life insurance can be purchased on the lives of the active participants

Techniques to Reduce Reversion

- Make certain that assets are not overvalued → particularly important for assets that are not publicly traded and for which a market value is not readily determinable
- Some advocate merging the plan with an underfunded defined benefit plan → be careful with this so as to avoid an abusive tax scheme

Thank you!