Proskauer

PBGC Issues Guidance on New Special Financial Assistance Program for Troubled Multiemployer Pension Plans

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As we previously reported, the American Rescue Plan Act of 2021 ("ARPA") created a special financial assistance program that is administered by the Pension Benefit Guaranty Corporation ("PBGC") and intended to extend the solvency of certain financially troubled multiemployer plans. The program provides special financial assistance ("SFA") to eligible plans in the form of one-time payments that are intended to allow the plans to continue to pay all benefits and expenses through 2051. As required by ARPA, on July 9, 2021, the PBGC issued an interim final rule (the "IFR") that provides clarity on the calculation and amount of SFA, the order in which eligible plans will be permitted to file SFA applications, certain procedural aspects with respect to the submission and review of SFA applications, and certain conditions and restrictions on plans that receive SFA. The IRS simultaneously published Notice 2021-38 to provide guidance on the impact of SFA on minimum funding, as well as issues related to the reinstatement of certain suspended benefits by plans that receive SFA, as required under ARPA.

This alert summarizes the key aspects of the PBGC and IRS guidance. More information surrounding the SFA program and the application process can be found on the PBGC's SFA website.

Eligibility

The PBGC projects that the SFA program will provide approximately $94 billion in SFA payments to more than 200 plans with approximately three million participants in total. Under ARPA, a multiemployer plan is eligible for financial assistance if it satisfies any of the following criteria:

- The plan is in "critical and declining" status in any plan year beginning in 2020 through 2022;

- The plan had a suspension of benefits in accordance with the MultiemployerPension Reform Act of 2014 (“MPRA”) as of March 11, 2021;
- The plan is in “critical” status in any plan year beginning in 2020 through 2022, has a “modified” funded percentage of less than 40%, and has a ratio of active to inactive participants that is less than 2:3; or
- The plan became insolvent after December 16, 2014, remains insolvent, and has not been terminated as of March 11, 2021.

The IFR provides a few clarifications on eligibility. As expected, the PBGC reiterated that a plan that terminated in a plan year that ended before January 1, 2020 is not eligible for SFA because it would not be subject to the special funding rules for endangered, critical, and critical and declining status plans in 2020, 2021, or 2022. In addition, the conditions for eligibility do not need to be satisfied in the same plan year. The PBGC also noted that a plan that elects to be in critical status under ERISA Section 305(b)(4), but does not otherwise meet the criteria for critical status under ERISA Section 305(b)(2), is not eligible for SFA.

Determining the Amount of SFA

The most eagerly anticipated aspect of the IFR was how the PBGC will calculate the amount of SFA available for eligible multiemployer plans. Under ARPA, the PBGC was given latitude to provide “such amount required for the plan to pay all benefits due during the period beginning on the date of payment of the special financial assistance payment and ending on the last day of the plan year ending in 2051.” The PBGC took a narrow interpretation of this language and determined that the amount of SFA is calculated after taking into account all of a plan’s existing and projected obligations and resources (including the present value of all future contributions, withdrawal liability payments, and other payments expected to be made to the plan through the plan year ending in 2051).

> ***Proskauer Observation:*** *A number of interested parties had suggested alternative methodologies that they viewed as more consistent with the legislative intent to provide a permanent solution to the issues faced by these troubled plans. However, the PBGC concluded that these proposed methodologies were not consistent with the statutory language and were ends-driven. While, under the PBGC's interpretation, ARPA still provides at least a temporary solution for decades, it is possible that some plans will not receive sufficient SFA to permanently avoid insolvency.*

The IFR provides specific definitions for the value of plan obligations, plan resources, and the date by which to make these determinations, defined as the "SFA measurement date" – which is the last day of the calendar quarter preceding the date on which a plan files an application for SFA.

The IFR also details the long-term interest rate and the assumed interest rate that the plans must use in their calculation. The assumed interest rate is the lesser of the interest rate used for funding standard account projections in the most recent zone status certification completed before 2021 or 200 basis points plus the third segment rate interest rate in the last four months prior to the filing of the application.

> ***Proskauer Observation:*** *This is particularly significant for plans that value liabilities with discount rates higher than the interest rate cap of 200 basis points plus the third segment rate. Those plans will be required to calculate the amount of their SFA based on the assumption that the SFA will earn the interest rate capped amount, and the use of the lower rate will allow the plans to receive more SFA. However, as noted below, the SFA can only be invested in investment grade bonds (or similar permissible investments), which are currently expected to earn far less. A number of interested parties had encouraged the PBGC to recognize this issue and use bifurcated interest rates, but it declined to do so. Thus, the viability of plans receiving SFA will depend in part on the investment returns of the non-SFA assets in the plan's portfolio.*

The IFR also contained significantly more information about the PBGC's approach to its review of plan assumptions other than the interest rate. An application that proposes changes to the assumptions from what was in the applicant plan's last zone status certification prior to 2021 will need to contain extensive data supporting the proposed assumption change, and the PBGC will give far more intensive scrutiny to changed assumptions. The PBGC's view appears to be that assumptions made after the passage of ARPA are more likely to have been influenced by a desire to increase the SFA.

> ***Proskauer Observation:*** *Coincident with its issuance of the IFR, the PBGC issued guidelines for assumption changes that plans can (but are not required to) use, if reasonable. These guidelines provide methodologies for extending assumptions to years that were not included in the zone certification (e.g., because the plan was projected to be insolvent before those years) and for changing assumptions generally. These guidelines are of particular relevance to plans that have experienced demographic or industry activity changes since the beginning of the COVID-19 pandemic.*

In other steps that appear to be designed to avoid what the PBGC viewed as artificially inflating the amount of SFA for which a plan is eligible, the IFR states that the amount of assistance cannot be increased by virtue of certain events occurring after the release of its guidance. These events include plan mergers, asset transfers, benefit increases (other than required restorations of benefit suspensions), and contribution decreases.

Content, Timing, and Review of Applications

The IFR contains detailed information about what must be included in an application, and there is further guidance in the application instructions and various templates that were issued by the PBGC contemporaneously with the IFR.

Regarding timing, ARPA requires that the PBGC process completed applications within 120 days of receipt. Recognizing that it may be difficult for the PBGC to timely process applications for all eligible plans at once, ARPA provided that the PBGC could elect to establish a priority application process for the most financially troubled multiemployer plans. Although multiple priority groups did not appear to be contemplated by the statute, the IFR contains six levels of priority, as described in the chart below. All other plans will be permitted to begin applying no later than March 11, 2023.

Priority Group	Description of Priority Group	Date Plans May Apply for SFA	Estimated Number of Plans
1	Plans already insolvent or projected to become insolvent before March 11, 2022	Beginning July 9, 2021	25
2	Plans that implemented a benefit suspension under ERISA § 305(e)(9) as of March 11, 2021 Plans expected to be insolvent within 1 year of the date an application for SFA is filed	Beginning January 1, 2022	18
3	Plans in critical and declining status that had 350,000 or more participants (*i.e.*, the Central States Pension Fund)	Beginning April 1, 2022	1
4	Plans projected to become insolvent before March 11, 2023	Beginning July 1, 2022	3
5	Plans projected to become insolvent before March 11, 2026	TBD, given 21 days warning, no later than February 11, 2023	22
6	Plans for which PBGC computes the present value of financial assistance under ERISA § 4261 to be in excess of $1 billion (in the absence of SFA)	TBD, given 21 days warning, no later than February 11, 2023	11

> ***Proskauer Observation:*** *The dates set forth in the above chart are somewhat malleable in that the PBGC may accelerate the date for a priority group depending on the number of applications submitted and other factors.*

The IFR also provides that an additional seventh priority group may be added, but the application deadline for such a group would be no later than March 11, 2023. The IFR allows for the processing of certain emergency filings beginning with priority group number two.

In addition to the priority groups, in order to ensure that it could timely review applications, the PBGC also included a "metering" approach to the acceptance of applications even within a priority group. Under this approach, once the PBGC accepts as many applications as it estimates it can process in the required time frame, it will temporarily close the electronic submission filing window and will not accept any additional applications. The IFR provides that the PBGC will provide notice of the opening and closing of the application portal if interested parties request to receive notice on the PBGC's website.

> ***Proskauer Observation:*** *The IFR appears to acknowledge that the metering approach is not provided for by ARPA, but the PBGC concluded that the metering is consistent with the PBGC's inherent authority to issue regulations related to the conduct of its business.*

If the PBGC denies an application for SFA, the agency is required to provide written notice of why the application was denied. A plan can elect to accept the denial and revise its application to cure the specific reasons for denial, rather than refile the entire application. In that case, no data can change other than that which resulted in the denial. A plan can also withdraw and resubmit its entire application, but it cannot change its "base data" (*i.e.*, SFA measurement date, participant census data, and interest rate assumptions) used for the initial application in any revised application.

> ***Proskauer Observation:*** *Requiring plans to maintain the same base data regardless of whether its application is denied or withdrawn will prevent a plan from withdrawing its application after a drop in asset values in order to increase its SFA.*

Payment of SFA

If a plan's application is approved, the IFR provides that the PBGC will typically pay out benefits in a lump sum within 60 days after approval and no later than 90 days after approval. The PBGC projects that the first SFA payment will be made by December 31, 2021.

> ***Proskauer Observation:*** *ARPA requires payment of SFA within one year of approval of a plan's application. Thus, under the IFR, payments will be made far more quickly than is required by the statute.*

The amount of SFA will be determined as of the SFA measurement date. Interest will then be added (at the funding standard account interest rate required in the plan's application) to account for the time between that date and the date of payment.

Restrictions on SFA

Pursuant to the authority provided for in ARPA, the IFR places certain restrictions on SFA funds that are given to a plan. Namely, SFA and any earnings thereon:

- May only be used to make benefit payments and pay administrative expenses;
- Must be segregated from plan assets; and
- Must be invested in investment-grade bonds or other certain permissible investments.

The IFR defines investment grade as "publicly traded securities for which the issuer has at least adequate capacity to meet the financial commitments under the security for the projected life of the asset or exposure." Permissible investments include individual fixed-income securities (including dollar-denominated foreign securities) and commingled vehicles (*e.g.*, exchange traded funds, mutual funds, pooled trusts, etc.) that invest in investment-grade bonds. The use of derivatives to replicate exposure or hedge is permissible as long as it does not increase credit or interest rate risk and the notional value of derivatives held in a separate account are supported by cash or dollar-denominated cash equivalents. Additionally, the IFR allows a plan to hold up to 5% of its SFA funds in investments that were considered investment grade at the time of purchase but are later downgraded below investment grade.

> ***Proskauer Observation:*** *The IFR stated that the PBGC recognizes the balance between the desire for security against the need to provide flexibility in overall investment policies. Thus, the IFR seeks comment on other investments that the PBGC could deem permissible. Interested parties concerned about the future viability of eligible plans, even with SFA, may want to consider commenting on this issue and suggesting higher returning alternatives.*

Importantly, the IFR provides that plans are permitted to use SFA to pay benefits and administrative expenses before using other plan assets.

> ***Proskauer Observation:*** *This is perhaps one of the most significant provisions in the entire IFR because it allows plans to preserve more of their other plan assets that are not subject to the foregoing investment restrictions. Had plans been required to use their non-restricted assets first, they would be forced to invest a growing proportion of their assets in a lower returning asset class for decades. This likely would have caused a number of plans to become insolvent prior to 2051 notwithstanding ARPA's stated intent.*

Conditions on SFA

As permitted by ARPA, the IFR also places certain conditions on plans that receive SFA as further described below.

- Withdrawal Liability: If an employer withdraws from a plan that receives SFA after the plan year in which the plan receives SFA, the employer's withdrawal liability must be calculated using the mass withdrawal interest assumptions under PBGC regulations. These interest assumptions must be used until the *later of*: 10 years after the end of the plan year in which the plan receives payment of SFA; or the last day of the plan year in which the plan no longer holds SFA or any earnings in a segregated account. For many plans, the use of these assumptions will inflate the dollar amount of an employer's allocable share of a plan's underfunding. However, SFA funds are also treated as plan assets for withdrawal liability purposes, which will help limit the impact of using these assumptions.

Proskauer Observation: *The IFR does not modify how an employer's withdrawal liability payment schedule is calculated. In many troubled plans, even with the SFA, many employers will be subject to the general 20-year cap on withdrawal liability payments absent a mass withdrawal. For those employers, this means that the foregoing changes may have no practical impact on their effective liability.*

We also note that the IFR contains a telling footnote stating that the PBGC intends to issue a separate, generally applicable rule — not limited to plans that receive SFA — that prescribes actuarial assumptions that a plan is required to use to calculate withdrawal liability. This issue has arisen in many withdrawal liability disputes over the years, so many plans and contributing employers will be watching closely any developments in this regard.

The IFR also provides that a plan entering a withdrawal liability settlement for a liability that exceeds $50 million (determined using the same mass withdrawal assumptions) must obtain the PBGC's approval to enter the settlement.

- Benefit Increases: During the SFA coverage period (*i.e.*, through the plan year ending in 2051), a plan that receives SFA may not adopt an amendment that provides a retroactive benefit increase other than any required reinstatements of suspended benefits. Prospective increases may be adopted during the SFA coverage period, but only if the plan actuary certifies that employer contribution increases are projected to be sufficient to fully pay for the increases, and provided that these increased contributions were not included in the determination of SFA.
- Contribution Decreases: Contribution rates for each contribution base unit cannot be less than, and the definition of contribution base unit cannot be different from, those set forth in the collective bargaining agreement or plan document in effect on March 11, 2021. There is an exception if the plan sponsor concludes that the reduction would lessen the risk of loss (*i.e.*, lowering the contribution requirement to avoid an employer going out of business entirely). However, PBGC approval is required if a reduction affects annual contributions over $10 million and over 10% of all employer contributions.
- Transfers or Mergers: During the SFA coverage period, a plan may not engage in a transfer of assets or liabilities (including a spinoff) or merger except with the PBGC's approval.
- Liquidity Requirement: During the SFA coverage period, plan assets, including SFA, must be invested in permissible investments (as described above) sufficient to pay for at least one year (or until the date the plan is projected to become insolvent, if earlier) of projected benefit payments and administrative expenses. Thus, even after the SFA is depleted, plans will have some investment restrictions.

- Reporting and Audit: Plans must submit an annual compliance statement and submit to audit by the PBGC regarding compliance with the ARPA requirements.

Reinstatement of Benefits

ARPA requires that a plan that receives SFA that previously suspended benefits in accordance with MPRA must reinstate its suspended payments and provide retroactive adjustments to affected participants and beneficiaries. The reinstatement of benefits is subject to oversight by the Department of Treasury and the PBGC. Thus, the IRS in conjunction with the PBGC issued Notice 2021-38 explaining the process for the reinstatement of benefits.

Pursuant to the requirements of ARPA, the make-up benefits must be made either as a lump sum within three months of the date of receipt of the SFA or in equal monthly installments over a period of five years, beginning within three months of the date the SFA is paid. The IRS Notice provides that a plan must be amended to reinstate the suspended benefits, provide for make-up benefits, and specify the form of distribution. The IRS Notice also clarifies that make-up benefits do not include actuarial adjustments (such as interest). An eligible plan may restore suspended benefits on a prospective basis prior to applying for SFA (but can only make the retroactive payments after the SFA application is approved).

The IFR and IRS Notice provide that ARPA's requirement for plans with suspended benefits to submit the application for SFA to the Department of Treasury will be satisfied if submitted to the PBGC in accordance with the PBGC's guidelines. Further, the IFR requires notice be provided to participants on the reinstatement of their benefits. The required contents of this notice can be found on the PBGC's website.

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The IFR and IRS Notice contains many additional requirements and nuances. Plans, employers, and other interested parties should consult with counsel regarding these details. The PBGC's website also provides a host of additional resources, model applications, and checklists regarding the SFA program.

Related Professionals

- **Ira M. Golub**
- **Robert M. Projansky**
  Partner
- **Justin S. Alex**
  Partner