Pension Benefit Guaranty Corporation

78-3

March 27, 1978

REFERENCE:
4063 Liability of Substantial Employer for Withdrawal
4063(b) Liability of Substantial Employer for Withdrawal. Amount of Employer Liability
4063(c) Liability of Substantial Employer for Withdrawal. Satisfaction of Liability Through Posting of Bond
4063(d) Liability of Substantial Employer for Withdrawal. Partitioning of Plan
4063(e) Liability of Substantial Employer for Withdrawal. Waivers
4064 Liability of Employers in Multiple Employer & Multiemployer Plans

OPINION:

This is in response to your request for a ruling on the application of § 4063 of the Employee Retirement Income Security Act of 1974 ("ERISA") to the anticipated withdrawal of * * * from the * * * Pension Plan (the "Plan"). The withdrawal will be a consequence of the proposed transfer of * * * service and facilities to * * * whose personnel participate in different pension plans. For the reasons given below, based on our correspondence and discussions with you and other * * * representatives, with Plan representatives and with representatives of the Maritime Administration, pursuant to § 4063(e) of ERISA the Pension Benefit Guaranty Corporation ("PBGC") has [*2] determined to waive the application of § 4063(b), (c) and (d) with respect to this withdrawal.

On the facts and circumstances of this case, we find that the Plan's funding arrangements constitute an indemnity agreement adequate to justify waiving the withdrawal Liability that might otherwise have been imposed under ERISA § 4063.

I. The Facts

* * *, which is a substantial employer (as defined in ERISA § 4001(a)(2)) with respect to the Plan, joined the Plan in 1971. * * *, which was acquired by * * * in December, 1969, had been a long-term but minor contributor to the Plan, and its last contributions were made in 1970. You have informed us that * * * operations, which necessitated * * * participation in the Plan, represent new service rather than a continuation of the former * * * operations. * * * Plan contributions increased from approximately $1 million in 1971 to approximately $2.1 million in 1977, and its share of total annual contributions rose from 5.7% to 13.8%. During that time, according to the actuarial reports you have furnished us, the Plan's total estimated unfunded liabilities declined from more than $224 million to almost $142 million.

The Plan's actuaries [*3] have estimated that, if the Plan had terminated August 1, 1977, the total value of unfunded benefits guaranteeable under Title IV of ERISA would have been about $80.4 million. As * * * average annual share of contributions over the preceding five years was 10.5%, under § 4064 of ERISA its pro rata share of that hypothetical insufficiency would have been about $8.46 million. * * * liability to PBGC would, however, have been limited to 30% of its net worth, as determined by PBGC.

Since 1965, the Plan has been funded on an actuarial basis, rather than at a fixed contribution rate. Section 30 of the current collective bargaining agreement, for example, requires full funding of past service liabilities over a 27-year period beginning June 16, 1975, and calls for quarterly reviews to assure that currently payable contributions are adequate to satisfy the employers' mutual obligation to amortize past service and fund current service liabilities. In addition, § 34(3) of the collective agreement requires a lump-sum payment representing estimated future contributions when the covered employment base is reduced as the result of the sale of ships.

Like * * * a number of contributing employers [*4] have Operating Differential Subsidy Agreements, pursuant to which the Maritime Administration underwrites the bulk of their Plan contributions. In the Plan year ending July, 1977, subsidized operators, including * * *, made 78.5% of all contributions. The major non-subsidized contributing employer was responsible for 14% of the contributions received last year.

While the Plan's financial status has improved in recent years, its contribution base has been shrinking. For example, last year an employer that had been responsible for slightly more than 8% of the contributions withdrew from the Plan; * * *, is now planning to withdraw and there is some doubt as to the continued participation of another subsidized carrier, which made more than 23% of the contributions in the 1977 Plan year.

II. Analysis

Under § 4063 of ERISA, a substantial employer that withdraws from a multiemployer plan must post security for satisfaction of its contingent liability to PBGC under § 4064 of ERISA. The amount of the security, which may be in the form of an escrow deposit or a bond, is measured by the amount for which the withdrawing employer would be liable if the plan terminated on the date [*5] of the withdrawal. The PBGC may realize on the security only if the plan terminates within five years after the withdrawal. The PBGC may waive the § 4063 security requirement, pursuant to § 4063(e), "whenever it determines that there is an indemnity agreement in effect among all other employers under the plan which is adequate to satisfy the purposes of [§ 4063] and of § 4064."

The basic purpose of termination liability, under § 4064 as under § 4062 of ERISA, is to protect PBGC's premium funds by requiring employers to reimburse the Corporation, to the extent of their capacity as indicated by their statutory net worth, if the termination of their pension plan gives rise to claims against the Title IV insurance system. Termination liability prevents employers that can continue funding a plan as required by ERISA from shifting their pension obligations to the PBGC's premium-payers.

The purpose of the § 4063 security requirement of ERISA is evident: it assures collectibility of a withdrawn employer's contingent debt to PBGC. Because § 4063 security payments cannot be used to pay pensions unless the plan terminates, the plan itself does not benefit from the bond/escrow requirements. [*6] Under appropriate circumstances, § 4063(d) gives PBGC discretion to assume certain Plan liabilities in order to strengthen the continuing plan. This partition option is only available upon a showing by the plan administrator that the decline in employer participation "has resulted, or will result, in a significant reduction in the amount of aggregate contributions to or under the plan by employers . . ." Plan partition has not been requested here and the facts before us do not indicate that it would be appropriate at this point.

To justify a waiver of the § 4063 security requirement, an indemnity arrangement need not expressly address the employers' responsibility for satisfying the withdrawn employer's contingent liability under § 4064 of ERISA. The remaining employers' commitment to fund all of the plan's liabilities in a responsible manner can satisfy the purposes of § § 4063 and 4064 by enhancing the prospects for plan continuation and reducing the PBGC's potential exposure if the plan later terminates. Indeed, the legislative history of § 4063(e) of ERISA indicates that Congress envisioned this type of indemnity agreement. In explaining the withdrawal liability provisions, [*7] the Conference Report on ERISA states:

The corporation is entitled to waive the use of either of these procedures if there is an indemnity agreement between all the other employers in the plan sufficient to satisfy all plan liabilities.

H. Rep. No. 93-1280, 93d Cong., 2d Sess. 379 (1974).

The Parties sponsoring the * * * Plan have departed from the typical multiemployer-plan pattern and agreed to full actuarial funding of the Plan's defined benefits, rather than negotiating a contribution rate that can only be changed through collective bargaining. Although Titles I and II of ERISA would have allowed 40 years to amortize the Plan's unfunded past service, the Union and the employers adopted a 27-year amortization schedule, and the collective agreement provides for timely adjustments to the employers' current payments to assure that the agreed-upon funding commitment is met. Moreover, § 34(3) of the collective agreement expresses the employers' commitment to protect the Plan directly from the potential adverse impact of certain actions that might reduce the Plan contribution base. n1 In our judgment these arrangements constitute an indemnity agreement within the contemplation [*8] of § 4063(e) of ERISA.

n1 We are aware that the enforceability of § 34(3) with respect * * * proposed transfer of services to * * * has been questioned. The availability of this collectively-bargained withdrawal liability, which could strengthen the Plan directly and to provide pension protection that is superior to the security requirements of § 4063, is relevant but not essential to the PBGC's determination in this case.

Whether a commitment among employers to continue funding an ongoing plan provides protection for the termination insurance system that is adequate to satisfy the purposes of § § 4063 and 4064 of ERISA depends, of course, on the likelihood that the continuing employers will honor that commitment. The actuarial reports you have submitted, and a series of employer-withdrawal notices that the Plan has filed, demonstrate that the * * * Plan's contribution base has been shrinking in recent years and that the decline could accelerate. As a result, per-day contributions have increased, and may increase further, to the extent future funding costs are not offset by payments under § 34(3) of the labor contract. Nevertheless the evidence is that the employers remaining [*9] in the Plan will be able to pay the increased contributions, either because the expense will largely be subsidized by the Maritime Administration or because of the companies' market strength. Thus, the potential increase in contributions is unlikely to precipitate full Plan termination in the near future.

Subsection 4063(e) gives PBGC discretion to waive withdrawal liability when it determines that there is a satisfactory indemnity agreement. In exercising that discretion, we evaluate the specific circumstances of a case in light of the purposes of Title IV of ERISA. In our judgment, the circumstances of the present case indicate that waiver is equitable and appropriate. This judgment is based on two major conclusions: first, that * * * withdrawal is a necessary consequence of a good-faith business arrangement, motivated in no way by the intent or desire to avoid pension obligations and second, that it is unlikely that the imposition of withdrawal liability here would be of sufficient benefit to either PBGC or the Plan to justify the unreasonable hardship it might pose for * * *

In connection with those conclusions, we note the following:

1. The transfer of * * * services [*10] to * * * must be approved in all respects by the Maritime Administration. If that agency approves, its determination will reflect an expert judgment that the transaction is bona-fide and will promote the policies of the Merchant Marine Act of 1936, 46 U.S.C. § § 1101 et seq., by strengthening U.S.-flag shipping.

2. * * * will continue defined-benefit pension coverage for the crews of the transferred vessels. That coverage will involve different multiemployer plans because of * * * collective bargaining obligations.

3. * * * would have no real financial incentive to withdraw from the Plan in order to avoid paying for its employees' benefits under the Plan, as * * * pension contributions are subsidized by * * * and would continue to be subsidized if * * * continued to employ Plan participants.

4. Given the improvement in the Plan's funding status during the years of * * * participation, it is possible that the Plan has profited from * * * short-term involvement. In effect, * * * has paid for the benefits that participants earned under the Plan as a result of their employment with * * *

5. In light of the substantial costs that PBGC would incur to determine and collect [*11] withdrawal liability from * * * and the impact of the net worth limitation on that liability, the net amount available as security for PBGC is not likely to be significant. On the other hand, the expense and regulatory complexities that * * * would face could endanger the transaction.

Please note that this letter-ruling relates solely to the application of § 4063 of ERISA. * * * will be liable to PBGC in accordance with § 4064 of ERISA if the Plan terminates within five years from the date of * * * withdrawal.

Matthew M. Lind
Executive Director