Pension Benefit Guaranty Corporation

81-10

May 5, 1981

REFERENCE:
4021(a) Plans Covered. Requirements of Coverage
4022 Benefits Guaranteed
4041(a) Termination by Plan Administrator. Filing of Notice of Intent to Terminate
4044 Allocation of Assets
4048 Date of Termination
4062 Liability of Employer in Single Employer Plans

OPINION:

This is in reference to your recent letters and telephone conversations with * * * of my staff regarding the above-referenced pension plan (the "Plan"). You ask whether the Plan is covered by Title IV of the Employee Retirement Income Security Act of 1974 ("ERISA"). You also have orally asked: 1) what date the PBGC will use for purposes of determining the employer's net worth, 2) whether the Plan allows contributions made to the Plan for the first plan year to be returned to the employer, and 3) whether the Plan authorizes payment of certain adminstrative expenses from Plan assets.

As we understand the pertinent facts, * * * Corporation adopted the Plan effective March 1, 1975, with Plan years commencing March 1 of every calendar year. On February 29, 1980, submitted a Notice of Intent to Terminate the Plan to the PBGC. You state that * * * submitted Form 5310 [*2] to the Internal Revenue Service in March 1980, and requested a favorable determination on termination with respect to the Plan. You state that the IRS had not previously issued, nor had * * * previously requested, a favorable determination letter with respect to the Plan.

You have stated that the IRS has not, at present, issued a determination letter and that the sole issue regarding qualification is whether the Plan discriminates in favor of officers, shareholders or highly compensated employees because of the absence of a benefit reduction formula provided for byRevenue Ruling 71-446. Section 401(a)(4) of the Internal Revenue Code provides that the contributions or the benefits of a qualified pension plan shall not discriminate in favor of employees who are officers, shareholders, or highly compensated (the "prohibited group" employees).The Plan does not incorporate the benefit reduction formula provided by section 5.02 ofRevenue Ruling 71-446. That section requires that if an employee at normal retirement date (or actual retirement date, if later) has completed fewer than 15 years of service, the maximum benefit percentage must be reduced by 1/15, or 2.5%, for each year of [*3] service less than 15 at such retirement date. n1 The effect of not includingRev. Rul. 71-446's benefit reduction formula is that the Plan's two prohibited group employees receive a greater benefit than they would under a properly integrated plan.

n1 Your letter stated that the employer intended to amend the Plan retroactively to include the reduction formula required for proper integration. You later indicated, in telephone conversations with Deborah West, that the amendment would not be adopted. Accordingly, this letter does not address the questions raised by your letter regarding the proposed amendment.

You have indicated that, in all other respects, the Plan met section 401's qualification requirements. n2

n2 We have discussed this matter with the IRS District Office and note that their position is consistent with that stated by you.

ERISA section 4021(a) provides that Title IV covers any plan, which, for a plan year --

(1) is an employee pension benefit plan (as defined in paragraph (2) of section 3 of this Act) established or maintained--

(A) by an employer engaged in commerce or in any industry or activity affecting commerce, or

(B) by any employee organization, [*4] or organization representing employees, engaged in commerce or in any industry or activity affecting commerce, or

(C) by both, * * * which has, in practice, met the requirements of part I of subchapter D of chapter 1 of the Internal Revenue Code of 1954 (as in effect for the preceding 5 plan years of the plan) applicable to plans described in paragraph (2) for the preceding 5 plan years; or

(2) is, or has been determined by the Secretary of the Treasury to be, a plan described in section 401(a) of the Internal Revenue Code of 1954, or which meets, or has been determined by the Secretary of the Treasury to meet, the requirements of section 404(a)(2) of such Code.

See also ERISA section 4022.

Based on the above-mentioned facts (and assuming a date of Plan termination under ERISA section 4048 in March 1980), the PBGC has determined that the Plan is covered under section 4021(a)(1) as of its termination date because the Plan in practice met the IRS plan qualification requirements during the five full Plan years prior to March 1980. During the Plan's existence, it was operated as a qualified plan. No officers, shareholders or highly compensated employees received benefits in excess [*5] of the amount to which they would be entitled under a properly integrated plan. Accordingly, the PBGC has determined that the Plan is covered by Title IV of ERISA.

This determination is subject to reconsideration under Subpart C of the PBGC's administrative review regulation. A copy of the regulation is enclosed. Your request for reconsideration must be submitted to the General Counsel within 30 days of the date of this letter. You are not required to file a reconsideration request in order to seek judicial review of this determination.

Upon the expiration of the reconsideration period or the disposition of a reconsideration request, we will refer this matter back to the Office of Program Operations to take appropriate action to determine whether the Plan has sufficient assets, when allocated in accordance with section 4044, to discharge when due all obligations of the Plan with respect to guaranteed benefits. n3

n3 Your letter discusses whether certain participants have benefits in priority category 6 of the section 4044 allocation. We need not address this issue at this time because it is unclear whether the plan has sufficient assets to pay all benefits guaranteed by the PBGC. [*6]

You have asked orally what date the PBGC will use to determine the employer's net worth for purposes of determining the amount of the employer's liability to the PBGC under ERISA section 4062. Normally the net worth record date is the date of plan termination, but the PBGC may chose a date that is up to 120 days prior to that date.See ERISA section 4062(b)(2). The ERISA section 4041(a) date of plan termination in the instant case is March 10, 1980.

You have indicated orally that, assuming that the Internal Revenue Service determines that the Plan is not qualified, the employer may, pursuant to Plan Article 11, seek to recover contributions made to the Plan for the first plan year. Article 11 provides, inter alia, that if the Internal Revenue Service determines "initially" that the Plan and Trust does not qualify under applicable sections of the Internal Revenue Code and the Employer decides not to amend the Plan or Trust to obtain qualified status, the Trustee shall return to the Employer all contributions made by it for the first plan year.

The Plan provision you cite does not authorize the return of the first year's contributions upon an IRS determination upon termination [*7] that the Plan is not qualified. Subpart (b) of Article 11 provides that "[u]pon return of the contribution for the first plan year by the Trustee [because of an IRS determination that the Plan does not initially qualify] the Plan and Trust shall terminate and the Trustee shall be discharged from all obligations" under the Plan. The provision, then, allows return of contributions when qualified status is denied to the ongoing plan (if the employer chooses not to amend the plan to obtain qualification). The provision provides for the subsequent immediate termination of the Plan. The provision is inapplicable here because the employer did not seek, nor did the IRS rule on, an initial determination of the ongoing Plan's qualification during the relevant period - i.e., during the Plan's life. n4 The provision's plain language indicates that it was intended to apply to the initial IRS determination with regard to the ongoing Plan; it does not apply to an IRS determination upon termination that the Plan does not meet the qualification rules in the Internal Revenue Code. Further, it is doubtful whether such a return is consistent with either Title I or Title IV of ERISA. We do not [*8] reach this issue, however, because the Plan language itself does not authorize the return.

n4 We note further, that the provision appears to contemplate that the employer will seek a determination of qualification from the IRS within an "initial" start up period. Thus, even were qualification sought with respect to the ongoing plan five years after the Plan was adopted, it is doubtful whether this provision would authorize the return of the first year's contributions.

You have stated in an April 20, 1981, letter to of this office that the Plan's Trustee, the Corporation, has directed that $15,000 in legal expenses and approximately $4,000 in actuarial expenses incurred in connection with the termination of the Plan be paid for with Plan assets.

As we have indicated orally, the PBGC cannot at this time approve use of Plan assets to pay these expenses. Plan Article 12.02(m) provides that "[t]he reasonable compensation for services due the Trustee, plus any reimbursement due for expenses, shall be paid by the Employer but if not paid by the Employer, shall be paid from the Trust Fund and the Trustee." This language indicates that the employer, not the Plan, is primarily responsible [*9] for the payment of expenses. The use of Plan assets to pay validly incurred reasonable Plan expenses must be consistent with the Trustee's fiduciary responsibilities under Title I of ERISA. For example, the use of Plan assets to pay expenses may not be reasonable if the employer has sufficient funds to pay those expenses and if no effort was made by the Trustee to obtain reimbursement of those expenses from the employer.

In the course of oral discussions with * * * you proposed that Plan assets representing the first year's contributions and the amount due for legal and actuarial fees be placed in escrow pending resolution of the issues regarding the first year's contributions and the payment of expenses. At the time of your proposal, an independent Trustee, the * * * Trust Company of * * * controlled Plan assets. The PBGC spoke with * * * of the * * * Trust Company on March 26, 1981, and indicated our view that as Trustee * * * Trust had a statutory duty to keep Plan assets intact. However, you have since informed us that, by resolution dated March 27, 1981 of the * * * Corporation Board of Directors, the * * * Company has been appointed to replace the Trust Company as Trustee. [*10] You have stated that, as the Leasing Corporation is now Trustee, you have no further interest in arranging for an escrow account. You have also indicated that you believe that the new Trustee may disburse Plan assets to pay for legal and actuarial fees, but will not return the first year's contributions to the employer.

n5 We note for your information that ERISA section 412 requires that each fiduciary of an employee benefit plan be bonded in accordance with that section.

The PBGC believes that the employer has not yet demonstrated that the Plan documents authorize actuarial and legal expenses incurred in connection with the Plan to be paid from Plan assets in this situation. The PBGC will, of course, consider any additional information you may wish to submit on this point.

We are prepared to discuss resolution of these matters. * * * is the attorney handling this matter. She may be reached by phone at (202) 254-3010.

Henry Rose
General Counsel