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One Minute Memo®

PBGC Announces New Enforcement Approach for Assessing Funding Liability upon Facility Shutdown or Other Cessation of Operations

Section 4062(e) of the Employee Retirement Income Security Act of 1974 (ERISA) imposes liability on a defined benefit plan sponsor that ceases operations at a facility if, as a result, more than 20% of active participants in the plan are separated from employment. The Pension Benefit Guaranty Corporation (PBGC), which insures pension benefits, is responsible for administering this liability. Historically, the PBGC enforced Section 4062(e) by requiring a sponsor of an underfunded defined benefit plan to make additional contributions to the plan or provide a financial guarantee in the event of a facility shutdown, regardless of the size of the plan or financial health of the sponsor. On November 2, 2012, the PBGC changed direction by announcing the implementation of a pilot program that focuses enforcement on companies that the agency determines to have a higher risk of default.

Under Section 4062(e), defined benefit plan sponsors are required to notify the PBGC if separations from employment due to a cessation of operations at a facility meet the 20% threshold described above. There are no formal rules defining a "cessation of operations," but in 2010 proposed regulations that were subsequently withdrawn, the PBGC indicated that Section 4062(e) may be triggered upon the voluntary or involuntary cessation of one or more of a plan sponsor's distinct organizational, operational or functional units at one or more facilities. Upon receiving this notification, the PBGC calculates the plan's underfunded liability triggered by the shutdown, and can require the sponsor to provide the PBGC with a bond or escrow amount based on such liability, or initiate a compromise settlement in lieu of requiring a plan contribution or the full bond or escrow amount. The new enforcement approach will reduce the number of plan sponsors having to enter into these negotiations by carving out from enforcement:

- Sponsors of plans with 100 or fewer participants; and
- Plan sponsors which the PBGC determines are "creditworthy."

The PBGC has announced that it will determine a company's creditworthiness based on common financial measures of financial soundness such as credit ratings, credit scores, indebtedness, liquidity and profitability. If a company is creditworthy and there are no other indicators of financial weakness or other risks, the PBGC will take no action. However, for up to five years after the facility shutdown, the PBGC may periodically request additional information from the company to confirm its creditworthiness. The PBGC may initiate enforcement action during this five-year period if it determines that the company is no longer creditworthy.

Please note, regardless of the new enforcement exemptions, all defined benefit plan sponsors are still required to notify the PBGC in the event of a facility shutdown resulting in the separation of more than 20% of active participants.

The new pilot program follows the PBGC's withdrawal of proposed Section 4062(e) regulations in 2010. The PBGC has now indicated that it will use the pilot program to determine what changes to make in future proposed regulations.

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