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PBGC regulations put the kibosh on spin-term premium reductions

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PBGC final regulations put a definitive end to the once-popular "spin-term" variable-rate premium (VRP) reduction tactic, while also formalizing the agency's ban on using the *de minimis* spinoff exemption to reduce flat-rate premiums (FRPs). The final regulations make few changes from the June 2019 proposal, but do provide a small number of new offerings aimed at simplifying requirements for ERISA Section 4010 filings and 4043 event reporting. This article highlights the key changes and clarifications in the final regulations. For a detailed discussion of the proposed regulations, see PBGC Proposal Squashes Spin-Terms, Includes Grab Bag of Other Changes (July 2, 2019).

Premiums

Like the proposed regulations, the final regulations take aim at popular premium-reduction strategies that relied on exceptions for some spinoffs and mergers.

Spin-term premium reduction strategy retroactively dead

Under 2014 final PBGC regulations, a terminating plan's sponsor owed no VRP in the year the plan distributed all assets. Some sponsors used this exemption to reduce their premiums by spinning off a portion of their plan, then terminating the original plan and distributing its assets in that same plan year. The sponsor paid no VRP for the terminated plan and only a pro-rated premium for the spun-off plan's short plan year. Under the new rules, this exemption is unavailable if the terminating plan engages in a non-*de minimis* spinoff during the premium payment year.

PBGC became loudly skeptical of this "spin-term" strategy in 2018, first expressing opposition in FAQs on its website and then again in that year's premium filing instructions. The agency then moved to formalize its stance in last year's proposed regulations. Commenters on the proposal asked for a prospective

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effective date, arguing the spin-term strategy was based on what many sponsors and practitioners felt was a legitimate reading of the prior rules. However, PBGC made the guidance effective retroactively, stating that its position is not a change in the rules, but simply a clarification of what the agency believes to be the "only reasonable" interpretation of the 2014 regulations.

By not including a prospective effective date, PBGC has opened the door to challenge prior premium filings that took advantage of the spin-term strategy. The agency has already reached out to some sponsors whose 2018 filings reflected a spin-term. It's not clear how diligently PBGC will challenge earlier spin-terms or if courts would side with the agency, since there arguably was no direct support for PBGC's position in the 2014 regulations (although the agency apparently thinks there is). Sponsors who might be affected by the retroactive application may want to consult with their legal counsel.

Terminating plan premium proration ban prospective only

The final regulations also permit prorating premiums in a short plan year, if it is a terminating plan's final year. This exception applies to both VRPs and FRPs, though it's irrelevant for VRPs because (as discussed above) a terminating plan doesn't owe VRPs for the year it distributes all assets. Like the VRP exception, the final regulations prohibit this proration if the plan engaged in a non-*de minimis* spinoff earlier in the year.

However, unlike the VRP exception, the short-plan-year proration ban applies prospectively only. This means that, if PBGC challenges past spin-terms, affected plans may only have to pay a portion of the VRP retroactively owed (if PBGC requests payment) rather than a full-year premium. The plan's prior filing will have already included a prorated FRP, so no additional FRP will be due.

De minimis merger clarification effective retroactively

The final regulations formalize PBGC's position that the merger of a large plan into a smaller one isn't *de minimis* (a stance already reflected in the 2020 premium instructions issued last November). This interpretation precludes sponsors from taking advantage of a special rule for *de minimis* mergers occurring at the beginning of the year. Under the special rule, the participant count date for the merged plan would remain the end of the previous plan year, ignoring participants that merged in from the larger plan and thereby producing a much smaller FRP.

As with the VRP exemption for terminating plans, the PBGC views this as a clarification of existing guidance. So there is no applicability date for this provision — meaning that this interpretation is effective retroactively. Sponsors that took advantage of this rule in prior years may want to consult with their legal counsel.

Reportable events

The final regulations leave largely intact the proposal's changes to the requirements for event reporting, including simplifications on the rules for active participant reductions, inability to pay benefits when due,

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and clarification of the low-default-risk waiver, among other items. The final regulations do have a few changes from the proposal, including:

- *A change in contributing sponsor is not automatically a reportable event.* The final rule clarifies that a change in the contributing sponsor is reportable only if the sponsor leaves the controlled group (when any member leaves the controlled group, it's considered a reportable event).

- *Disclosures by parent companies treated as if made by contributing sponsors.* The final rules provide that disclosures by a parent company are treated as if those disclosures were made by a plan's contributing sponsor, if the parent company is a public company within the same controlled group. The treatment applies in two circumstances: for the extension of the deadline to disclose a liquidation until it is disclosed on an SEC Form 8-K or in a public press release, and for the public company waiver for five reportable events. The rule also clarifies that the public company extension for liquidation events is available to a foreign private company that issues an English-language press release in the US.

4010 filings

The final regulations made only a few changes from the proposal for 4010 reporting:

- *Exempt entities excluded when determining whether an organizational chart is required.* The final regulations maintain the proposal's requirement to file an organizational chart when a filer is part of a controlled group with more than 10 members. But the regulations clarify that exempt entities are disregarded when determining whether there are more than 10 members. The organizational chart may include or exclude exempt entities.

- *Cash balance plans don't need to reflect anticipated changes in mortality.* The regulations keep the proposed reference chart summarizing required assumptions for determining a plan's benefit liability, but the chart now specifies that plans may disregard anticipated changes in mortality for years after the information year, for purposes of converting account balances to annuities. The chart also includes a category for other assumptions (such as cost-of-living increases and marital status) apparently omitted from the proposed regulations by accident.

- *Plans may disregard at-risk status for the $15 million shortfall waiver.* The proposal would have required plans to use the special at-risk assumptions when determining the funding target for purposes of the $15 million shortfall waiver, if the plan was at-risk for funding purposes. But after commenters raised a number of practical objections, PBGC will now permit a plan to disregard at-risk status, concluding that this simplification is unlikely to extend the waiver to plans it wasn't intended to cover.

- *Elimination of proposed waiver for late funding-balance elections.* PBGC's proposal would have provided sponsors a reporting waiver if the sole cause of the plan's failing the 80% gateway test was

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a late election to reduce its funding (credit) balance. Commenters raised several questions regarding the practical application of this waiver, and in response, PBGC chose to eliminate the waiver, concluding that it would have been helpful to few filers, if any. Instead, PBGC suggests that sponsors in this situation request a case-specific waiver.

Effective dates

Except as noted above for certain clarifications to the rules for premiums, the new regulations are effective prospectively. Changes to 4010 filing requirements are generally effective for filings made or amended on or after April 15, 2020, though the changes for valuing benefit liabilities are applicable for plan years beginning on or after Jan. 1, 2020 (or earlier, at the sponsor's discretion). Changes to event reporting are effective for events occurring on or after March 5, 2020.

Related resources

Non-Mercer resources

- Final rules: Miscellaneous clarifications, corrections and improvements (Federal Register, Feb. 4, 2020)
- Proposed PBGC rules: Miscellaneous corrections, clarifications and improvements (Federal Register, July 27, 2019)

Mercer Law & Policy resources

- PBGC kills premium-reduction tactic for mergers, requires more e-filings (Nov. 6, 2019)
- PBGC simplifies 4010 controlled-group filing requirements (Oct. 17, 2019)
- PBGC proposal squashes spin-terms, includes grab bag of other changes (July 2, 2019)

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