

The Inside Scoop on Pension Plan Termination

WHAT TO KNOW BEFORE YOU START

Frequently Asked Questions | Webcast 12.5.18

FAQ

Answers to the following questions are for standard plan terminations, not distress terminations.

FINANCIAL READINESS

1 What is Liability Driven Investing (mentioned during the risk management strategies comments)?

Liability Driven Investing or LDI is a bond matching approach to risk management. First, look at the duration of your liabilities and make sure the duration of your assets match those. If the interest rates go up, your assets are going to go down and so will your liabilities. Basically, this strategy gets your assets and liabilities to start moving in tandem from the perspective of protecting your funded status.

2 Is the plan termination projection tool *Findley PlanTerm™ Financial Modeler* available?

We will share it with you in person. It is a pretty intricate tool and requires some plan specific programming on our end, but we only need some cash flow information from you to make that happen. Once we receive the needed data, we would be happy to meet with anyone that wants to see a demonstration and view different scenarios for their specific plan.

3 What is a settlement?

A settlement is an accounting calculation of a one-time charge/(credit) through income of the unrecognized loss/(gain) that is on the balance sheet. You have to run the loss/(gain) through income when you do plan termination accounting and zero everything out on the balance sheet.

4 Who are the top two buyers to approach for a plan with approximately \$50 million in obligations?

That is a big question and really brings up some other issues as well.

- » **Who are the biggest annuity providers?** It depends on how you measure it but certainly Prudential, Mass Mutual, and AIG would be three of the larger providers.
- » **Can I sell my pension plan?** Citigroup and Prudential looked into offering that option several years ago but the IRS would not allow such a transaction.
- » **If the plan is not ready to terminate, is it a good idea to purchase annuities for all retirees before terminating the plan?** NO! Don't purchase annuities for all retirees if plan termination is in your near future. You can do a more limited annuity purchase ahead of plan termination. However, your experience, when you terminate the plan, will be best if you have some retiree benefits to include with the deferred benefits when seeking annuity bids to close out the plan. There are several companies that are unable to terminate their plans because the insurance companies are not interested in bidding on deferred only groups. Those plans, with deferred only lives, will have to continue to maintain their plans until they get a sufficient number of retirees to attract a quote and/or are able to entice members with a lump sum window.

5 Is Accumulated Other Comprehensive Income (AOCI) accounting tracked in the *Findley PlanTerm™ Financial Modeler*?

The modeler currently projects the cash funding level and how different economic conditions affect it. The accounting aspects are not included in the modeler.

Once a plan sponsor is seriously thinking about a plan termination, we would certainly work with them to make sure they understand the AOCI.

6 If your plan is already overfunded, what's the best way to address that?

First, make sure it is overfunded on a plan termination basis, which is a different measurement than either pension funding or accounting reporting measurements. If the plan is overfunded on a plan termination basis, there are a few ideas to address all or some of the overfunding:

- » The fees incurred in terminating a pension plan are significant, and most can be paid from plan assets as long as the plan document does not prohibit payment of expenses from the trust. That would include the fees for actuarial work, legal counsel, annuity consulting, administration assistance, etc.
- » The 50% excise taxes on any assets that revert to the plan sponsor can be reduced to 20%, in the case of a for-profit entity, in one of three ways:
 - By sharing at least 20% of the excess assets with the participants on a pro rate basis.
 - By directly transferring at least 25% of the excess assets to a qualified replacement plan, as long as at least 95% of the active participants in the terminating plan also participate in the replacement plan.
 - By showing evidence that the plan sponsor was in Chapter 7 bankruptcy liquidation (or similar proceeding under state law) on the date of plan termination.

Seek the guidance of your ERISA counsel on these ideas, and be sure to clearly document how you treat the excess.

DATA READINESS

7 Regarding data quality, what do you mean by certified benefits, and who should certify the final benefits?

Having “certified” benefits means the calculations are final and not estimates. The actuary, plan sponsor, or third party plan administrator can validate that the calculations are final.

8 How do you address data quality when purchasing annuities?

As we prepare benefits for the plan termination and eventual lump sum payout or annuity purchase, we work closely with the sponsor to collect and review data making sure we have names, Social Security numbers (SSNs), address information, and data needed to support the calculations. Most often, we will keep a master database with notes regarding qualified domestic relations orders (QDROs), incomplete data, and deaths, etc. and address them on a case by case basis.

9 How do you deal with members for whom you have no SSN?

We, of course, ask for the plan sponsor to look through their files, benefit records, life insurance forms or any other place that an SSN might be recorded. If we are unable to locate the SSN, and we still can't find the member, he or she will be turned over to the Pension Benefit Guaranty Corporation (PBGC) lost participant program. If we can locate the member and that member does not have an SSN, he or she can apply for a tax identification number using IRS form W-7 that can be used in lieu of the SSN.

COMMUNICATIONS PREPAREDNESS & PROJECT PLANNING

10 How do you find out what needs to be in the communications?

There are model notices out there for most of the required communications that will be part of the plan termination itself. However, they are very dry, with only the legally required language. You'll have best results when you consider these to be a part of your total retirement program communications. Use your company or benefits program branding so they are easily recognizable as important, and take advantage of the time to add additional information to head off some of the question volume and even influence behaviors.

11 Who needs to be included in the project planning to get ready?

Internally – Typically the CFO and/or VP of Finance, CHRO/VP of HR/Director of HR, In-house General Counsel, and those empowered to make decisions/do advising for the plan and resources that would be allocated to the ongoing project of getting ready to terminate the plan

Externally – ERISA Attorney, Actuary, Investment Advisor, Annuity Consultant, Third Party Administrator

OTHER TOPICS

12 What is a partial plan termination?

Partial plan termination sounds similar to a termination, but it is a very different scenario. It is triggered when you terminate a group of participants (think downsizing for example). As a result, you may have to vest some of the participants that are not vested. A partial plan termination is not getting rid of the plan; it is about termination of employees vs. plan termination. Plan termination eliminates all liabilities and turns them over to an insurance company or to the participants. They sound related but are actually two different things.

13 Is it better to terminate a plan or freeze it to new members?

These are two different decisions. A plan freeze is a decision regarding your retirement program in general. Determine if you want to freeze your benefits and start providing benefits under a different program, maybe defined contribution. A termination would typically follow some time after the freeze. You could consider terminating right after a freeze, if ready, but most plan sponsors do that a few years down the road.

14 What is involved when you are audited?

Most likely if a plan gets audited, you are going to be looking at a PBGC audit. All plans over 300 members are audited and about one third of the plans under 300 members are audited by the PBGC. You may also be audited by the IRS or DOL. In general, during an audit, you receive a letter that says you have been selected for audit. It will ask you for several pieces of information, most likely including copies of your initial notice of intent to terminate, the notice of plan benefits, plan document information, including your most recent determination letter, amendments, the final trust statement showing all the assets are zeroed out, etc. All the elements that were part of the plan termination and benefit calculations will be reviewed. They will likely come back with additional questions. Hopefully, your approach to organized documentation through the plan termination process will make your audit relatively painless.

15 Can lump sum cash outs be offered to all participants, even those with a certified benefit exceeding a specific amount?

Yes, lump sums can be offered to all participants. There are certain situations where lump sums can be limited (for example, 415 limits and top 25 employees). However, in most cases there aren't any statutory limits that apply to lump sum cash outs. Some plans will limit lump sums to only be available when the lump sum is below a certain threshold (for example, \$25,000), but this is a plan specific limit that can be eliminated with a plan amendment.

If you have additional questions, please contact
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