United States General Accounting Office

GAO

Report to the Honorable Claudine Schneider, House of Representatives

September 1990

PENSION BENEFITS

Processing of Applications by the Pension Benefit Guaranty Corporation

GAO/HRD-90-127

United States
General Accounting Office
Washington, D.C. 20548

Human Resources Division

B-237725

September 25, 1990

The Honorable Claudine Schneider
House of Representatives

Dear Representative Schneider:

This report responds to your request that we provide information on four cases involving pension benefit applications processed by the Pension Benefit Guaranty Corporation (PBGC). The applications were submitted by participants in plans for which PBGC assumed responsibility after they terminated with insufficient assets.

Established by the Employee Retirement Income Security Act of 1974 (ERISA), PBGC administers an insurance program that guarantees participants' earned benefits at plan termination. PBGC insures the benefits of nearly 40 million workers in approximately 102,000 private pension plans. When a plan terminates with insufficient funds to pay promised benefits, PBGC generally takes over and administers the plan. Between 1974 and 1989, PBGC paid benefits for a total of 1,441 plans. In 1989, PBGC paid about $356 million in benefits to about 109,000 participants.

Results in Brief

In two of the four cases reviewed involving pension plans now administered by PBGC, the Corporation in 1989 and 1990 reversed its previous denials of benefits. PBGC now either has provided or plans to provide benefits to the affected participants. We concur with the reversals. As a result of PBGC's reconsideration of one of these two cases, two participants previously denied pension benefits are now eligible for benefits and an estimated 73 other participants will receive increased benefits.

In the third case, PBGC was correct in denying survivor benefits because, at the time the plan terminated, ERISA did not require that survivor benefits be paid if the participant died before reaching the earliest retirement age.

In the fourth case, PBGC delayed providing benefits to participants in two plans because the Internal Revenue Service (IRS) took over a year to provide PBGC with needed tax information. PBGC officials told us such delays are common. However, they had not attempted to resolve the problems with IRS' National Office. After we brought the problem to the attention of IRS officials, they started actions to ensure that PBGC receives requested information within 90 days. These actions should

Recognition of Vesting Amendment Benefits Additional Workers

One of the denial cases we reviewed involved a participant in a plan that had adopted an amendment incorporating ERISA's 10-year vesting standard just before terminating in 1976. The participant had enough years of service to vest under ERISA's standard but not under his plan's previous standard. However, PBGC did not recognize the plan's amendment and denied benefits to the participant. Subsequently, after settling a class-action lawsuit that required it to more fully recognize ERISA-mandated vesting standards, PBGC concluded that the plan's vesting amendment is valid. As a result, the individual whose case we reviewed, as well as at least one other participant who was previously denied benefits, are now eligible. In addition, an estimated 73 participants in related plans will receive benefit increases.

Minimum Vesting Standard Recognized

The participant whose case we reviewed had 10-1/2 years of service before leaving his job in February 1976 at age 59. He participated in the company's collectively bargained pension plan for union workers; a second plan covered nonunion workers. Both plans required participants under age 65 to work at least 15 years to be vested; participants with fewer than 15 years received no benefits.

The company filed for reorganization under bankruptcy law in July 1976. As part of its reorganization plan, it closed one of its plants and terminated portions of its pension plans in October 1976.[3] Two days before the termination, the company signed an agreement with the union that amended the collectively bargained pension plan, effective retroactively to January 1, 1976, to comply with ERISA's minimum 10-year vesting standard.

Since 1981, the worker in this case has been requesting pension benefits from PBGC. He has argued that, because he met the minimum 10 years required for vesting, he should be entitled to benefits beginning in April 1982, when he reached age 65. PBGC, however, did not recognize the 10-year vesting provided in the October 1976 plan amendment because the amendment had not been in effect for a year prior to plan termination.

[3]Workers who lost their jobs because of the plant closing, as well as those who had already left the company, were assigned to two terminated plans. Workers in the plant that continued in operation were placed in two continuing plans. The continuing plans terminated with insufficient funds in 1979.

PBGC Agrees to Include Plan Under Settlement Agreement

PBGC had not included the plan involved in the case we reviewed under the Rettig settlement agreement. We found, on review of this case, that an amendment to comply with ERISA vesting standards had been agreed to by the company and the union before the plan terminated. We questioned why PBGC was not considering the amendment in calculating benefits.

PBGC officials had not applied the terms of the Rettig settlement to the plan because they were uncertain whether the October 1976 agreement had been adopted before the plan terminated. The agreement needed the approval of the bankruptcy court to be effective. PBGC officials told us that when they initially processed the case, they did not determine whether the bankruptcy court had granted approval. Having since reviewed the case file, in February 1990 PBGC officials concluded that the bankruptcy court had granted approval.

PBGC now takes the position that the plan amendment was adopted prior to termination and will honor an effective date of January 1, 1976. All participants who had earned 10 years of service on or after that date are entitled to benefits, including the individual whose case we reviewed. At least one other participant previously denied eligibility also had over 10 years of service. For the plans that terminated in 1979, PBGC originally applied the 10-year vesting standard as of March 3, 1978. Because PBGC has accepted the retroactive effective date of January 1, 1976, an estimated 73 participants in these plans will receive benefit increases.

These individuals will begin receiving benefits or benefit increases once PBGC calculates them, PBGC officials told us. We believe PBGC's decision to provide benefits to these individuals is consistent with the terms of the Rettig settlement.

Insured Survivor Benefits Limited for Plans Terminated Before 1984

Two of the cases we were asked to review involved denials of survivor benefits. Under ERISA, pension plans offering annuities (for example, monthly payments) are required to allow their retiring married participants to elect a joint and survivor annuity. If the participant dies, the spouse receives an annuity that is at least 50 percent of the participant's pension amount. The joint and survivor annuity, which usually pays reduced benefits, is automatically provided unless declined.

ERISA originally provided limited protection for spouses of vested pension plan participants who died before receiving their pensions. Plan

them if PBGC did not properly notify them of their eligibility. If the eligible participant has died, surviving spouses will receive benefits. On the basis of this policy, PBGC reversed its denial and paid both the participant's estate and the surviving spouse, as if the participant had elected early retirement benefits.

We agree with PBGC's denial in the case of the participant who died before reaching the earliest retirement age. Under the ERISA provisions in effect when the plan terminated (1979), the spouse was not eligible for survivor benefits because the participant was not yet eligible for benefits at the time he died.

Benefit Payment Regulations May Help Applicants Understand PBGC Decisions

Although ERISA was enacted 16 years ago, PBGC has not yet issued benefit payment regulations. According to PBGC officials, PBGC has placed a higher priority on developing regulations for premium collection, management of insurance funds, and processing plan terminations. PBGC plans to release its first benefit payment regulations for public comment in April 1991.

Describing PBGC policies and procedures in regulations will better inform applicants about the benefit payment process and applicable laws and policies, PBGC officials believe. For example, many surviving spouses, such as those in the two cases we reviewed, may mistakenly believe that REA protects them if participants die after REA's enactment, PBGC officials told us. They believe these regulations would clarify that benefit insurance is based on the plan termination date.

Benefit Payments Delayed Because IRS Did Not Provide Timely Information

The fourth case involved participants who complained that PBGC took too long to begin paying benefits. Retirees who were receiving benefits before the termination continued to receive them from existing plan assets. But 8 to 10 newly eligible retirees waited for their benefits for up to 16 months after the plans terminated. Over half of the delay occurred because PBGC was waiting for tax returns from IRS.

To avoid making erroneous benefit payments to participants in plans that may have sufficient assets, PBGC begins paying new retirees only after it confirms that the plan's assets are insufficient and that it should take responsibility for paying the plan's benefits. In examining plan finances, PBGC asks companies for such documents such as tax returns, financial statements, and corporate records. PBGC officials told us that tax returns are the most reliable source in determining whether a

Agency Comments

We obtained written comments from PBGC. In a letter dated July 25, 1990 (see app. I), PBGC took issue with our description of its actions in one case. Specifically, PBGC did not agree with our statement that, at the time of our review, PBGC had not included the plan involved in the first denial case as part of the Rettig settlement agreement. (See p. 5.) PBGC stated that on May 8, 1989, prior to our review, it already had determined that this plan was to be included.

Information that PBGC provided does not support its statement. In a May 8, 1989, letter, PBGC advised a contractor responsible for reviewing plans that

> "The plan is now to be considered potentially Rettig-Affected and further research will be required to determine if the vesting in the Agreement complies with all aspects of ERISA vesting."

Further, during our review PBGC officials told us on several occasions that they had not yet determined whether the plan in question should be included under the agreement. As we note in our report, PBGC officials said they were uncertain whether an agreement amending the plan's vesting schedule to meet ERISA's minimum standards had been approved by the bankruptcy court. (See p. 5.)

PBGC provided us with a memorandum, dated February 26, 1990, in which PBGC's Office of General Counsel concluded that the agreement had been approved by the bankruptcy court. On March 8, 1990, PBGC officials told us that this memorandum provided the information they needed to include the plan under the settlement. As a result, the participant whose case we reviewed is now eligible for benefits.

PBGC also disagreed with our description of the effects of two laws on the benefits which PBGC provides. We have clarified the text as appropriate to reflect PBGC's concerns, which did not affect our assessments of their handling of the cases we reviewed. (See p. 15).

Mr. Gregory J. McDonald, page two

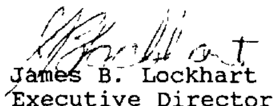
plans, not one plan that was "partially terminated" as indicated on page 5. Two of the resulting plans were terminated in 1976, and the two continuing plans were terminated in 1979. During the course of reviewing plans subject to the Rettig/Piech Settlement Agreement, PBGC re-examined the October 1976 pension agreement, determined that it was adopted in October 1976 rather than in a restated plan document dated in 1978, and reversed its earlier determination. As a result, two participants who were participants in a Washburn Wire pension plan that terminated in 1976 are entitled to benefits under the Rettig/Piech Settlement Agreement. As a further result of the PBGC's re-examination of the validity of the October 1976 pension agreement, 73 participants in a Washburn Wire pension plan terminated in 1979 will receive increased benefits.

In two other major respects, your draft is legally inaccurate. First, in referring to the Multiemployer Pension Plan Amendments Act of 1980 (MPPAA) on page 6, you state, "As a result of this legislation, PBGC no longer phases in benefit increases designed to comply with ERISA minimum standards." That statement is not correct. MPPAA did not change the phase-in provisions of ERISA, but merely permitted ERISA minimum standards to be read into unamended plans.

Second, your discussion of the legal effect of the Retirement Equity Act (REA) and its preretirement survivor protection (pages 9-11) is misleading. As you correctly state, the PBGC may legally pay benefits only in accordance with the law in effect on the plan termination date. REA expanded the preretirement survivor protection for on-going plans; but, contrary to the implication in your discussion, it did not expand the PBGC guarantee to cover such death benefits. Of the two spouses in question, one is entitled to a surviving spouse's benefit (not a preretirement survivor annuity) since the participant could have elected early retirement in the form of a 50% joint and survivor annuity before his death. The other is not entitled to a benefit, since the participant died before becoming entitled to any benefit under the plan.

Thank you for the opportunity to comment on your report. If you have any questions with respect to my comments, or would like to arrange a meeting, please contact Mr. Steve Hill of my staff on (202) 778-8810.

Sincerely,



James B. Lockhart
Executive Director

Ordering Information

The first five copies of each GAO report are free. Additional copies are $2 each. Orders should be sent to the following address, accompanied by a check or money order made out to the Superintendent of Documents, when necessary. Orders for 100 or more copies to be mailed to a single address are discounted 25 percent.

U.S. General Accounting Office
P. O. Box 6015
Gaithersburg, MD 20877

Orders may also be placed by calling (202) 275-6241.

Major Contributors to This Report

Human Resources Division, Washington, D.C.

Robert F. Hughes, Assistant Director, (202) 535-8358
Cynthia M. Fagnoni, Assignment Manager
Paul C. Wright, Evaluator-in-Charge

Office of General Counsel, Washington, D.C.

Suzanne M. Stover, Attorney

Comments From the Pension Benefit Guaranty Corporation

Pension Benefit Guaranty Corporation
2020 K Street, N.W., Washington, D.C. 20006-1860

Office of the Executive Director

July 25, 1990

Mr. Gregory J. McDonald
Associate Director
United States General Accounting Office
441 G Street, N.W. Room 6739
Washington, D.C. 20548

Dear Mr. McDonald:

This is in response to your draft report concerning questions raised by the Honorable Claudine Schneider.

The draft report contains inaccuracies and omissions in its discussion of participants in the Washburn Wire pension plans and the PBGC's initial denial of benefits to two of those individuals. The discussion implies that PBGC discovered an error and reversed its decision as a result of GAO's audit. The report fails to explain that these pension plans, along with several hundred others, are included in a court approved agreement in settlement of a class action suit (PBGC v. Rettig/Piech). The Rettig/Piech Settlement Agreement provides benefits previously denied under the agency's rules on phase-in of benefit increases.

The GAO has not fully considered the implications of the Rettig/Piech Settlement Agreement, which affects cases terminated and processed by the PBGC between 1976 and 1981. As a result of this agreement, PBGC is reviewing these previously terminated cases, including Washburn Wire, and identifying people eligible for benefits under the agreement. On May 8, 1989, the PBGC had already made a determination that the Washburn Wire pension plans were to be included in the plans covered by the Rettig/Piech Settlement Agreement. The PBGC then transmitted this information to its contractors and requested that they make the appropriate changes prior to the start of GAO's audit. Therefore, your statement on page 7 that "PBGC had not included the plan involved in this case under the Rettig settlement agreement" is erroneous.

Further, we find that your discussion of the October 1976 Washburn Wire pension agreement, concerning an amendment to the plans, and the PBGC's inquiry into the amendment's legal validity are not accurately presented in your report. The Washburn Wire Pension Plans were partitioned under ERISA § 4063(d) into four

Contents

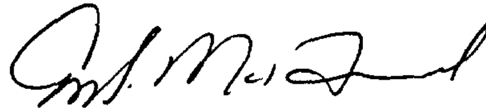
Letter	1
Appendix I Comments From the Pension Benefit Guaranty Corporation	14
Appendix II Major Contributors to This Report	16

Abbreviations

ERISA	Employee Retirement Income Security Act of 1974
IRS	Internal Revenue Service
PBGC	Pension Benefit Guaranty Corporation
REA	Retirement Equity Act of 1984

As agreed with your office, unless you publicly announce its contents earlier, we plan no further distribution of this report for 30 days. At that time, we will send copies of the report to interested congressional committees, the Executive Director of PBGC, the Commissioner of Internal Revenue, and other interested parties, and will make copies available to others on request. If you have any questions concerning this report, please call me at (202) 275-6193. Other major contributors to the report are listed in appendix III.

Sincerely yours,



Gregory J. McDonald,
Associate Director,
Income Security Issues

related corporate entity could assume responsibility for the plan or whether corporate assets exist that could help pay unfunded benefits. PBGC first asks the company for the tax returns. If it is unable or unwilling to provide them, PBGC requests the returns from IRS.[7]

In this case, the company refused to provide tax returns. In August 1987, PBGC asked the IRS district office that had geographical jurisdiction over the returns to provide the company's corporate returns and the company president's individual returns for the latest 3 years. IRS did not submit the returns to PBGC until September 1988. After receiving and analyzing the returns, PBGC took responsibility for the two plans and made back payments to the affected retirees.

Long delays in receiving returns from IRS are common, PBGC officials told us. In some cases, IRS may not send the returns to PBGC at all. PBGC did not receive returns in 10 of 20 cases that it recently reviewed to assess how quickly IRS responded. The two longest outstanding requests were made 3 years ago. In the remaining cases, IRS responded within 3-9 months. Without tax returns, PBGC officials told us that they had to base their decision on whether to take responsibility for the plan on other, less reliable sources of company financial information.

Plan to Develop Procedures to Speed Transfer of Tax Returns

We visited IRS National Office officials to discuss the reasons for the delays and lack of responses. These officials told us that they were unaware that there was a problem; PBGC officials confirmed that they had not notified the IRS National Office of this situation. IRS subsequently learned that PBGC had been sending some requests to IRS field offices, which were not responsible for supplying the returns. This resulted in requests having to be rerouted or handled by staff unfamiliar with PBGC's access to returns.

IRS and PBGC began to develop procedures for handling the requests in March 1990. IRS officials have prepared a listing of appropriate IRS disclosure offices to which PBGC should send requests for returns. The listing also identifies IRS officials whom PBGC should contact if a requested return is not sent. By using these procedures, IRS officials told us, PBGC should receive the returns within 60-90 days after a request is made. These procedures should help ensure that eligible participants receive the benefits due them as quickly as possible.

[7]PBGC has access to tax returns in administering the termination insurance program under IRS Regulation 301.6103(l)(2)-3

sponsors were required to give them survivor benefits only if the deceased participants had (1) reached their earliest date of retirement or were within 10 years of normal retirement age (whichever was later), (2) continued to work for the company after the earliest retirement date, and (3) elected an early survivor benefit. PBGC insured only preretirement survivor benefits already being paid when the pension plan terminated.

Retirement Equity Act Expanded Preretirement Survivor Protection

The Retirement Equity Act of 1984 (REA) expanded protection for preretirement benefits. Plans now must provide automatic survivor benefits to the spouse of any vested participant who dies before retirement, regardless of the participant's age at death. Participants may decline this coverage, as well as joint and survivor coverage, only with the spouse's consent. REA's preretirement survivor provision generally was made effective for all covered participants who worked at least 1 hour on or after August 23, 1984, the day REA was enacted.[6]

The two cases we reviewed involved participants who had not been receiving pension benefits when they died. One participant had reached the earliest retirement date but had not applied for benefits; the other died before reaching the earliest retirement date. Although both participants died after REA was enacted, their pension plan terminated in 1979, 5 years before REA became effective.

The two spouses were not covered by REA's protections because PBGC pays benefits according to the laws in effect at the time of plan termination. Based on ERISA provisions in effect at the time the plans terminated, only the participant who was eligible for early retirement benefits could have elected them and been receiving benefits at the time he died. However, PBGC had no record of his applying for benefits. With no evidence that he had applied, PBGC ruled that his spouse was not eligible for a survivor annuity.

One Denial Reversed Because of Notification Requirement

Both surviving spouses questioned PBGC's ruling. In reviewing the cases, PBGC found that it may not have notified the participant who was eligible for early retirement benefits of his eligibility. Under PBGC policy, participants who did not apply for early retirement benefits receive

[6]PBGC believes that REA did not expand the PBGC benefit guarantee to cover such benefits. However, PBGC policy states that the Corporation is committed to providing preretirement coverage in terminated plans similar to that which ongoing plans must now provide.

Under ERISA, PBGC insurance coverage is phased in for those benefit increases that have been in effect less than 5 years before a plan terminates; increases in effect for less than 1 year are not insured. PBGC considered plan amendments that adopted ERISA's vesting standards to be a type of benefit increase. As a result, PBGC concluded that the participant was not vested because he did not have the required 15 years of service.

In 1980, the Congress enacted legislation[4] that authorized PBGC to guarantee benefits based on the minimum standards of ERISA, even if plan provisions did not meet the minimum standards. PBGC concluded that ongoing plans should be treated as having complied with ERISA's minimum standards on the date originally required—the start of a plan's first year after December 31, 1975. For plans terminating after December 31, 1981, these standards would have been in place for at least 5 years. As a result, PBGC has fully recognized the minimum vesting standards for plans terminating after December 31, 1981, with no phase-ins.

Settlement Required PBGC to Pay Benefits Previously Denied

Participants in plans terminating after ERISA became effective, but before PBGC implemented the 1980 legislative change, challenged PBGC's interpretation of ERISA's phase-in rule. In the class action lawsuit, Rettig v. PBGC,[5] participants whose plans had adopted ERISA minimum vesting standards prior to termination sued PBGC for benefits denied because PBGC had phased in ERISA-mandated vesting improvements. They argued that amendments designed to comply with ERISA should not be considered a benefit increase.

In 1987, PBGC settled the case by agreeing to pay affected participants and beneficiaries 65 percent of the benefits due them without computing the phase-in. PBGC agreed to accept the earlier of the adoption or effective date, back to January 1, 1976.

[4]The Multiemployer Pension Plan Amendments Act of 1980 (P.L. 96-364, Sept. 26, 1980).

[5]Rettig v. PBGC, 744 F.2d 133 (1984).

alleviate similar problems regarding delayed benefit payments to participants in the future.

Background

The Congress enacted ERISA to protect the benefits of participants in private pension plans. ERISA established minimum vesting standards, which provided that the longest a plan could require a participant to wait before being fully vested was 10 or 15 years. Plans providing full vesting at 15 years were required to partially vest participants beginning after 5 years and to increase the vested amount each year by a specified minimum percentage until full vesting was achieved. These minimum standards were effective for plan years beginning after December 31, 1975.[1]

In addition, ERISA established an insurance program to help ensure that plan participants and their beneficiaries receive their earned benefits should their plans terminate. If a defined benefit pension plan[2] terminates, ERISA requires PBGC to provide timely and uninterrupted pension payments. After receiving a termination notice, PBGC analyzes the information pension plan administrators are required to submit to determine if plan assets are sufficient to pay the guaranteed benefits. If a plan has insufficient assets, PBGC generally becomes trustee of the plan and assumes responsibility for paying benefits. As part of the trusteeship process, PBGC audits plan records to establish participants' entitlement to guaranteed benefits. PBGC is required to notify participants of their guaranteed benefits and their right to appeal PBGC's initial determination of these benefits.

Scope and Methodology

The four cases we reviewed involved pension plans for which PBGC assumed responsibility after the plans had terminated with insufficient assets. To assess PBGC's handling of these cases, we interviewed PBGC and IRS officials and obtained and reviewed pertinent information from PBGC's case files and case processing procedures. We also analyzed recent court cases involving vesting issues. We did our work between August 1989 and March 1990 in accordance with generally accepted government auditing standards.

[1] For plan years beginning in 1989, participants generally must be fully vested in 5 to 7 years.

[2] In a defined benefit pension plan, the benefits are established in advance by a formula, based on such factors as years of employment, retirement age, and compensation.