AMERICAN BENEFITS COUNCIL

August 25, 2017

Regulatory Affairs Group
Office of the General Counsel
Pension Benefit Guaranty Corporation
1200 K St., NW
Washington, DC 20005-4026

Dear Sir or Madam:

On behalf of the American Benefits Council (the "Council"), I am responding to the Request for Information from the Pension Benefit Guaranty Corporation ("PBGC") published in the Federal Register on July 26, 2017 regarding input on regulatory and deregulatory actions that PBGC should consider as part of its regulatory program.

The Council is a public policy organization representing principally Fortune 500 companies and other organizations that assist employers of all sizes in providing benefits to employees. Collectively, the Council's members either sponsor directly or provide services to retirement and health plans that cover more than 100 million Americans.

We thank PBGC for requesting input and are grateful for PBGC's openness to a dialogue with the community. More broadly, PBGC's leadership in engaging with the community on defined benefit plan issues is very much appreciated.

EARLY WARNING PROGRAM

While we greatly appreciate the ongoing dialogue we have had on the Early Warning Program ("the Program"), we strongly believe the Program needs a complete review in the context of regulatory reform.

Of all of PBGC's programs, the Program has perhaps the greatest potential to disrupt the normal operation of the American businesses to which it is applied. Yet the Program operates without any statutory or authorizing regulatory guidance. In other words, it is a creation of an agency without any direct legal authority.

We are particularly concerned the Program has been established and operated in violation of the Administrative Procedure Act ("APA") because the Program has never been subject to a formal notice and comment regulatory process. Under the APA, "legislative" rules may only be established following a notice and comment regulatory process. Although the APA does not provide a clear bright-line test for determining when an agency's action is a "legislative" rule as opposed to "non-legislative" rule, the D.C. Circuit has opined that an agency rule's status as a "legislative" rule turns on "the prior existence or non-existence of legal duties and rights."[1] Also, as the Third Circuit observed, "[i]f the Guidelines have a substantial adverse impact on the challenging party, they are 'legislative.'"[2] The Program undoubtedly is a rule that creates new duties for affected employers and it can also have substantial adverse impacts on targeted employers when, for example, they are required to make cash contributions that are not otherwise required by ERISA's minimum funding requirements or when they are required to grant a security interest in company assets to PBGC.

At the very least, the Program continues to exist and evolve in violation of the principles announced in the Office of Management & Budget's ("OMB") Final Bulletin for Agency Good Guidance Practices (the "Final Bulletin"), which requires a public notice and comment process for economically significant "guidance" documents. (Economically significant "guidance" documents include any agency guidance disseminated to regulated entities or the general public that may reasonably be anticipated to lead to an annual effect on the economy of $100 million or more. At the very least, PBGC's published guidance on the Program constitutes economically significant guidance due to the Program's annual effect on the economy in excess of $100 million). Although "guidance" rules, like "non-legislative" documents, are not generally subject to the APA's notice and comment requirements, the Final Bulletin extends notice and comment procedures to "economically significant" agency guidance unless an agency head identifies a particular document, in consultation with OMB's Office of Information and Regulatory Affairs ("OIRA") Administrator, for which notice and comment would not be feasible or appropriate. We are not aware of any such exemption considered with regard to the Program, and even if it were granted, we question the notion that a notice and comment process would not be feasible or appropriate.

The Final Bulletin referenced above has a very telling description of the exact issue at stake here:

> Because it is procedurally easier to issue guidance documents, there also may be an incentive for regulators to issue guidance documents in lieu of regulations. As the D.C. Circuit observed in Appalachian Power:
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>> The phenomenon we see in this case is familiar. Congress passes a broadly worded statute. The agency follows with regulations containing broad language, open-ended phrases, ambiguous

[1] Am. Min. Cong. v. Mine Safety & Health Admin., 995 F.2d 1106, 1110 (D.C. Cir. 1993).
[2] Chao v. Rothermel, 327 F.3d 223, 227 (3d Cir. 2003).

> standards and the like. Then as years pass, the agency issues circulars or guidance or memoranda, explaining, interpreting, defining and often expanding the commands in regulations. One guidance document may yield another and then another and so on. Several words in a regulation may spawn hundreds of pages of text as the agency offers more and more detail regarding what its regulations demand of regulated entities. Law is made, without notice and comment, without public participation, and without publication in the Federal Register or the Code of Federal Regulations.

> Concern about whether agencies are properly observing the notice-and-comment requirements of the APA has received significant attention. The courts, Congress, and other authorities have emphasized that rules which do not merely interpret existing law or announce tentative policy positions but which establish new policy positions that the agency treats as binding must comply with the APA's notice-and-comment requirements, regardless of how they initially are labeled.

In the context of today's emphasis on regulatory reform, we believe that the time has come for the Program to be set aside until a proper regulatory process has been completed.

Without the regulatory process, PBGC retains the unchecked power to ask for concessions in exchange for not involuntarily terminating a company's plan, which would have devastating effects on the company. In our April 24th letter to PBGC, we included a number of ways to check that power, but those suggestions were not taken. This is a serious issue that deserves the scrutiny of the regulatory process.

PBGC USE OF FINANCIAL SOUNDNESS IN REGULATORY AND ENFORCEMENT INITIATIVES

We are very concerned about the recent use of the financial soundness of the plan sponsor as a factor in PBGC's exercise of its enforcement and interpretive authority. We ask that this factor be deleted from the current reportable events regulations, which would need to be substantially reformed, and not be used in any other PBGC regulatory, enforcement, or legislative initiative.

Pro-cyclical nature of the financial soundness test. There are two main reasons for the long decline of the private defined benefit plan system. First, the increasing volatility of plan funding and accounting obligations makes business planning and capital planning exceedingly difficult, especially for public firms. Second, the funding and accounting rules have a "pro-cyclical" effect, so that when economic challenges are the greatest, the burdens are the highest. Companies concerned about making inevitable future down cycles far worse may need to consider exiting the system. Use of a financial soundness test exacerbates the second problem.

Financial soundness test is a threat to PBGC. One very clear fact is often overlooked in analysis of threats to PBGC. No healthy company has ever turned over liabilities to PBGC. Only unhealthy companies pose a risk to PBGC. So logically, PBGC's primary interest should be to help financially challenged companies recover so they do not have to turn over their obligations to PBGC. While we appreciate that the use of financial soundness as a trigger for additional burdens may appear logical on the surface, if applied in practice, it makes it more difficult for plan sponsors to recover and thus (1) increases the likelihood of liabilities being turned over to PBGC and (2) is not in the best interests of plans or participants.

Financially strong companies oppose the use of financial soundness tests. Many financially strong companies have expressed grave concerns to the Council about PBGC's use of financial soundness as a trigger for increased burdens.

First, such companies know that they could face business challenges in the future. Currently strong companies do not want burdens imposed in the future when they are least able to afford such burdens. Further, a company may have a very strong plan and experience short term business challenges.

Second, strong companies that want to stay in the system know that the pro-cyclical effects of the financial soundness tests will cause many more plan sponsors to exit the system. That would mean that far fewer companies would be responsible for paying for PBGC liabilities, thus dramatically increasing the burden for those companies.

Additional reasons that both strong and less strong companies have expressed opposition to PBGC assessing the financial soundness of private companies are discussed further below.

Financial soundness tests led to de-risking and will lead to more de-risking. For the reasons described above, the imposition of financial soundness tests is a contributing factor to the trend toward plan shrinkage by offering lump sums or providing annuity contracts—generally referred to as "de-risking." In fact, it was the Administration's PBGC premium proposal—based on a financial soundness test—that provided the original catalyst for de-risking. Additional rules that include financial soundness tests increase risk for sponsors maintaining pension plans, and thus will push companies to further de-risking.

Inappropriate for PBGC to assess the financial soundness of businesses. It is inappropriate for PBGC, on behalf of the Federal government, to judge the financial soundness of companies. There has been some suggestion that the proposed test is simply based on existing commercial measurements, but that is not accurate. In every case, PBGC has gone far beyond existing commercial measurements in its reportable events regulation. Every one of the seven financial soundness factors in the regulation was wholly the creation of PBGC. Here are two examples. The “no loan default rule” was created by PBGC and does not take into account meaningless technical defaults that are waived by the lender and are not indicative of any business issue. The “two years of positive net income” test was also created by PBGC. And it does not make sense. For example, very profitable companies can have one-time events that result in a misleading loss year. Additionally, the application of this rule to non-profits is simply inconsistent with the nature of non-profit organizations.

PBGC TRANSPARENCY

For too long, PBGC has reported a deficit for its single employer plan program based on assumptions that are created purely by PBGC itself. This has led to widespread misunderstanding of the true financial condition of PBGC and has accordingly led to questionable policy decisions. **PBGC can and should publish its reports on its financial condition based on the same assumptions that Congress has imposed on private plans.** The interest rate and mortality assumptions applicable to private pension plans (but without pension smoothing) should also apply to PBGC.

For PBGC, the most accurate measurement of its liabilities may be based, at least in part, on the projections it does in connection with its projections reports. For these purposes, PBGC rejects many of the assumptions underlying its reports on its current financial condition and makes more realistic assumptions based on stochastic modeling, such as regarding future investment experience. It is very puzzling why PBGC would use one set of assumptions for projecting its future financial condition and very different assumptions for reporting on its current condition.

In the interest of transparency, PBGC should report on its current condition in two ways: (1) based on the assumptions applicable to private plans, and (2) based on the assumptions underlying PBGC’s own projections. Currently, PBGC uses an opaque methodology that is unrealistically conservative, substantially overstating its liabilities.

INTEREST PAYMENTS ON PREMIUM OVERPAYMENTS

The PBGC Participant and Plan Sponsor Advocate addressed this issue very well in her 2016 report:

> Another outstanding issue that needs regulatory guidance involves the PBGC payment of interest on premium overpayments. This issue was originally raised in the Advocate’s 2014 Annual Report. Provisions of the Pension Protection Act of 2006, enacted over ten years ago, allow the payment of interest on premium overpayments (even on a retroactive basis). PBGC has expressed the view that it must adopt regulations implementing its authority to pay interest on overpayments. PBGC has committed on a number of occasions to issuing these regulations, which would go a long way in balancing the scales when PBGC exacts interest

> on late premiums, and may have the positive effect of causing PBGC to work more expeditiously in resolving premium overpayments.

PBGC charges interest on premium underpayments and should pay interest on premium overpayments, consistent with the authorization Congress gave PBGC to do so for all periods on or after August 17, 2006 (even on a retroactive basis). Premium overpayments occur in a wide variety of circumstances, including where (as can happen with premium underpayments) there is a simple and inadvertent mistake that may affect the premium calculation for several plan years.

Overpayments of the flat-rate premium frequently occurred in connection with the estimated flat-rate Form 1-ES premium filings for large plans. Although such filings were no longer required for 2014 and later plan years, interest should be paid for overpayments relating to such filings for pre-2014 plan years. Other situations in which premium overpayments occur, and in which interest should be paid, include those involving estimated variable-rate premium filings (as explicitly allowed under PBGC regulations), premiums paid for non-covered plans (either because of a mistaken belief that the plan is covered or simply to guard against penalties while PBGC is considering a request for a determination of non-coverage), the standard termination exemption from the variable-rate premium (where a standard termination is initiated during a plan year and completed near the end of the plan year), and proration of the premium for a short plan year (where the length of the short year is not yet known when the premium is paid).

Payment of interest on premium overpayments is long overdue and we ask PBGC to prioritize addressing this issue.

<u>REPORTABLE EVENTS: LOAN DEFAULTS</u>

Again, the Advocate has addressed this issue very well in her 2015 report:

> [T]here are aspects of the [reportable event] rules that may create difficulties for the regulated community. For example, the final rule greatly expands reporting of loan defaults by requiring reporting even if the default is technical in nature, even if it is cured, and even if the default does not occur because the lender waives the default or agrees to the amendment of a covenant, the effect of which is to cure or avoid a breach that would trigger default. This will require much more monitoring on the part of plan sponsors to ensure that even the most technical defaults, and even certain non-defaults, are reported pursuant to the regulations. And this may also lead to problems in connection with representations and warranties, notice requirements, default provisions, and cross-default provisions under a variety of corporate loan or other agreements.

This issue merits PBGC attention. In particular, because of the obvious difficulties for sponsors and plan administrators in trying to keep track of all technical defaults and even of various “non-defaults” under the new rules, PBGC should provide appropriate waivers (which PBGC has the authority to grant, even on an across-the-board basis, without undergoing a rulemaking proceeding) to limit the monitoring and reporting burden to where it is fully warranted.

<u>REPORTABLE EVENTS: FOREIGN AND FOREIGN-LINKED ENTITIES</u>

For almost 20 years, PBGC’s reportable events regulations recognized that it is often difficult for a plan sponsor or plan administrator to be aware at all times of events involving foreign non-parent entities or “foreign-linked entities” (*i.e.*, U.S. entities that are linked to the sponsor only through foreign ownership), or even to know of the controlled group relationship with such an entity. Accordingly, until the new rules went into effect in 2016, PBGC provided a very useful reporting extension, applicable to several reportable events, until 30 days after the sponsor or plan administrator had “actual knowledge” of the event and of the controlled group relationship.

The new PBGC rules no longer include that extension and, as a result, reporting is now due within 30 days after the sponsor or plan administrator “knows *or has reason to know*” that the reportable event has occurred (which implicitly entails knowledge or constructive knowledge of the controlled group relationship). This change was not discussed by PBGC in any of the rulemaking preambles that led to the new rules, and no rationale has been provided by PBGC as to the reason why the change was made.

The newly-applicable constructive knowledge standard that now applies makes it difficult for sponsors and plan administrators to have comfort as to their obligations. PBGC should consider either granting relief similar to that provided under the old rules, or at least providing specific guidance as to what steps PBGC would consider adequate in guarding against delinquencies (and possible penalties that may be assessed) based on an assertion that a sponsor or administrator who didn’t “know” of the reportable event somehow had “reason to know” of the reportable event.

We thank you for your consideration of the issues addressed in this letter. We would like to meet to discuss these issues and will be reaching out to you soon in this regard.

Sincerely,

Lynn D Dudley

Lynn D. Dudley
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